No. 92-466

In The

Supreme Court of the United States

October Term, 1992

LIGGETT GROUP INC.,
now named Brooke Group Ltd.,

Petitioner,

vs.

BROWN & WILLIAMSON
TOBACCO CORPORATION,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Fourth Circuit

JOINT APPENDIX
VOLUME I, PAGES 1-273

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(*For Complete Appearances See Reverse Side Of Cover*)

Petition For Certiorari Filed September 16, 1992
Certiorari Granted November 16, 1992

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KEY

In this Joint Appendix, brackets indicate text added by counsel to inform the Court of appropriate notations or other information not appearing on the face of the document itself. Where the date of a document has been derived by reference to its accompanying testimony, the citation (Tr. ___:___) to such testimony has been included with the document's date.

CHRONOLOGICAL LIST OF RELEVANT DOCKET ENTRIES

UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF NORTH CAROLINA

DATE	FILING OR PROCEEDING
7-2-84	Plaintiff's Complaint filed.
7-17-84	Plaintiff's Verified Supplemental & Amended Complaint with Jury Demand filed.
7-24-84	Answer, Counterclaim & Motion to Strike of Defendant, Striking Allegations in Paragraph 50 of Verified Supplemental & Amended Complaint filed.
7-24-84	Defendant's Motion for Summary Judgment filed.
7-24-84	Defendant's Brief in Support of its Motion for Summary Judgment with attached: Affidavit of Charles G. Lamb. Affidavit of M. Lance Reynolds. Affidavit of Norwood Robinson. Affidavit of T.E. Sandefur, Jr.. Affidavit of J. Kendrick Wolls, III.
8-14-84	Plaintiff's Answer to Defendant's Counterclaim filed.
8-14-84	Plaintiff's Memorandum in Opposition to Defendant's Motion for Summary Judgment with attached: Affidavit of Herbert Pease filed.

Affidavit of Josiah S. Murray.
Affidavit of E.C. Bryson, Jr.

8-21-84 Defendant's Reply Brief to Plaintiff's Memorandum in Opposition to Defendant's Motion for Summary Judgment.

8-21-84 Second Affidavit of Charles G. Lamb, in Support of Defendant's Reply Brief to Plaintiff's Memorandum in Opposition to Defendant's Motion for Summary Judgment.

8-30-84 Hearing before Magistrate Sharp on Discovery Matters, Defendant's Motion for Summary Judgment, Defendant's Motion for Protective Order & Defendant's Motion to Strike Affidavit.

11-30-84 Magistrate's Sharp's Findings and Recommendations: recommended that Defendant's Motion for Summary Judgment be denied, without prejudice to its renewal after first-stage discovery period.

2-5-85 Order of Judge Bullock, Pursuant to Magistrate's Findings and Recommendations, that Defendant's Motion for Summary Judgment is denied with respect to all 5 claims in Plaintiff's Supplemental and Amended Complaint, Defendant can renew Motion for Summary Judgment within 60 days at close of Discovery.

3-7-85 Answer of Defendant Brown & Williamson to Plaintiff's Second Amended Complaint with Counterclaims against Liggett Group Inc. and Generic Products Corp.

3-27-85 Plaintiff Liggett's Reply to Defendant Brown & Williamson Tobacco Corp.'s Answer to Second Amended Complaint & Counterclaims.

5-1-85 Counterclaim Defendant Generic Products' Motion to Dismiss for Failure to State a Claim upon which Relief can be Granted, etc.

5-1-85 Counterclaim Defendant Generic Products' Memorandum in Support of Motion to Dismiss with attachments including: Affidavit (Unsigned) of Herbert L. Pease, in Support.

8-1-86 Plaintiff's Motion for Leave to Amend its Verified Supplemental & Amended Complaint.

8-1-86 Plaintiff's Memorandum (Sealed) in Support of Motion for Leave to Amend its Verified Supplemental & Amended Complaint including the Affidavit (sealed) of Philip T. Shannon.

9-10-86 Defendant Brown & Williamson's Memorandum (Sealed) in Opposition to Plaintiff's Motion for Leave to Amend its Complaint.

10-1-86 Plaintiff Liggett's Reply Brief (Sealed) to Brown & Williamson's Memorandum in Opposition to Liggett's Motion for Leave to Amend its Verified & Amended Complaint.

1-2-87 Defendant Brown & Williamson's Motion for Summary Judgment on all claims in the Complaint of Plaintiff Liggett Group, Inc. filed with:
Affidavit (Sealed) of Kenneth G. Elzinga.
Affidavit of Lanny W. Butler.
Affidavit (Sealed) of Lanny W. Butler.
Affidavit (Sealed) of B.E. Bacon.
Affidavit (Sealed) of Roman L. Well.
Affidavit (Sealed) of M. Lance Reynolds.
Appendixes (Sealed).

1-2-87 Defendant Brown & Williamson's Memorandum of Law (Sealed) in Support of its Motion

for Summary Judgment on Liggett's Robinson-Patman Act Claim.

1-2-87 Defendant Brown & Williamson's Memorandum of Law (Sealed) in Support of its Motion for Summary Judgment dismissing Liggett's Price Discrimination Claim in its Entirety.

1-2-87 Brown & Williamson's Memorandum of Law (Sealed) in Support of its Motion for Summary Judgment on Liggett's Trademark and Unfair Competition Claims.

1-5-87 Plaintiff Liggett's Motion for Summary Judgment on its Fifth Cause of Action.

1-5-87 Plaintiff Liggett's Memorandum (Sealed) in Support of Motion for Summary Judgment filed with:
Affidavit (Sealed) of William H. Hogeland.
Affidavit (Sealed) of Bruce Topman.

1-5-87 Plaintiff Liggett's Motion for Judgment on Defendant Brown & Williamson's Counter-Claims.

1-5-87 Plaintiff Liggett's Memorandum (Sealed) in Support of Motion for Summary Judgment on Defendant Brown & Williamson's Counter-Claims filed with the Affidavit (Sealed) of Adam C. Barker.

2-2-87 Plaintiff Liggett's Memorandum (Sealed) in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment Dismissing Liggett's Price Discrimination Claim.

Plaintiff Liggett's Memorandum (Sealed) in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment on Liggett's Trademark & Unfair Competition Claims (Sealed).

2-2-87 Plaintiff Liggett's Memorandum (Sealed) in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment on Branded Versus Generic Cigarettes.

2-2-87 Affidavit (Sealed) of William H. Hogeland, in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment & in Further Support of Plaintiff Liggett's Motion for Summary Judgment.

2-2-87 Affidavit (Sealed) of Bruce Topman, in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment & in Further Support of Plaintiff Liggett's Motion for Summary Judgment.

2-2-87 Affidavit (Sealed) of Joseph Diamante, in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment on Liggett's Trademark & Unfair Competition Claims.

2-2-87 Affidavit (Sealed) of William B. Burnett, in Support of Plaintiff Liggett's Opposition to Defendant Brown & Williamson's Motion for Summary Judgment.

2-2-87 Affidavit (Sealed) of Thomas F. Keller, in Support of Plaintiff Liggett's Opposition to Defendant Brown & Williamson's Motion for Summary Judgment.

2-2-87 Affidavit (Sealed) of David R. Jackson, in Support of Plaintiff Liggett's Opposition to Defendant Brown & Williamson's Motion for Summary Judgment.

2-2-87 Defendant Brown & Williamson's Memorandum (Sealed) in Opposition to Plaintiff Liggett's Motion for Summary Judgment on Liggett's Fifth Cause of Action.

2-2-87 Defendant Brown & Williamson's Memorandum (Sealed) in Opposition to Plaintiff Liggett's Motion for Summary Judgment dismissing Brown & Williamson's Counter-Claims.

2-2-87 Affidavit (Sealed) of Rachel Pollock in Support of Defendant Brown & Williamson's Opposition to Plaintiff Liggett's Motion for Summary Judgment.

2-2-87 Affidavit (Sealed) of Kenneth G. Elzinga, in Support of Defendant Brown & Williamson's Opposition to Plaintiff Liggett's Motion for Summary Judgment.

2-19-87 Plaintiff Liggett's Memorandum (Sealed) in Reply to Defendant Brown & Williamson's Memorandum in Opposition to Liggett's Motion for Summary Judgment on its Fifth Cause of Action.

2-19-87 Plaintiff Liggett's Reply Memorandum (Sealed) in Support of its Motion for Summary Judgment on Defendant's Counter-Claims.

2-19-87 Reply Affidavit (Sealed) of Adam C. Barker, in Support of Plaintiff Liggett's Motion for Summary Judgment on Defendant's Counter-Claims.

2-19-87 Affidavit (Sealed) of Garret G. Rasmussen, in Support of Plaintiff Liggett's Motion for Summary Judgment.

2-19-87 Reply Affidavit (Sealed) of William H. Hogeland, in Support of Plaintiff Liggett's Motion for Summary Judgment.

2-19-87 Reply Affidavit (Sealed) of Kenneth G. Elzinga, filed by Defendant Brown & Williamson in Response to 1-30-87 Affidavit of William B. Burnett.

2-20-87 Defendant Brown & Williamson's Reply Memorandum (Sealed) in Support of Motion for Summary Judgment on Liggett's Robinson-Patman Act Claim Regarding Sales of Branded Versus Generic Cigarettes.

2-20-87 Defendant Brown & Williamson's Reply Memorandum (Sealed) in Support of Motion for Summary Judgment on Liggett's Trademark & Unfair Competition Claims.

2-20-87 Defendant Brown & Williamson's Reply Memorandum (Sealed) in Support of Motion for Summary Judgment dismissing Liggett's Price Discrimination Claim in its Entirety.

3-25-87 Affidavit (Sealed) of Martin Flumenbaum, in Support of Defendant Brown & Williamson's Motion for Summary Judgment Dismissing in its Entirety Price Discrimination Claim of Plaintiff.

4-16-87 Notice of Oral Argument on Dispositive Motions at 9:30 a.m. May 12, 1987 in Greensboro.

5-11-87 Supplemental Affidavit (Sealed) of William H. Hogeland, submitted by Plaintiff Liggett in Support of their Motions for Summary Judgment & in Opposition to Brown & Williamson's Motions for Summary Judgment.

5-12-87 Hearing before Magistrate Sharp on Dispositive Motions. Hearing continued throughout the day. Hearing to be continued to a date to be set. Transcript to be sealed when filed.

5-12-87 Deposition (Copy) (Sealed) of William B. Burnett, filed by Defendant Brown & Williamson in Support of Dispositive Motions.

5-15-87 Notice of Oral Argument on Dispositive Motions at 9:30 a.m. on June 3, 1987 (continued from May 12, 1987).

5-22-87 Affidavit (Sealed) of Harold A. Grant, in Support of Plaintiff Liggett's Motion for Summary Judgment in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment.

5-22-87 Affidavit (Sealed) of K.v.R. Dey, Jr., in Support of Plaintiff Liggett's Motion for Summary Judgment and in Opposition to Defendant Brown & Williamson's Motion for Summary Judgment.

6-3-87 Hearing before Magistrate Sharp in Greensboro. Plaintiff's Motion for Summary Judgment on Defendant's Counterclaim is heard and taken under consideration.
Plaintiff's Motion for Summary Judgment on Defendant's Counterclaim is heard and taken under consideration.
Plaintiff's Motion to Admit Affidavit's of Dey and Grant are taken into consideration (Oral Motion)
Defendant GPC Motion to Dismiss is taken under consideration.

12-15-87 Findings & Recommendations of Magistrate Sharp, Brown & Williamson's Motion for Summary Judgment on Liggett's Trademark & Unfair Competition Claims Denied except as Liggett requests legal relief with respect to Brown & Williamson's use of infringing Leaf Design mark; Liggett's Motion to Amend to add further Trademark & Unfair Competition Claims Denied; Brown & Williamson's Motion for Summary Judgment on Liggett's Robinson-Patman Claim as to Branded v. Generic Granted; Brown & Williamson's Motion for Summary Judgment on Liggett's Robinson-Patman Claim as to Generic v. Generic Denied; Liggett's Motion for Summary Judgment on its Robinson-Patman Claims Denied; Liggett's Motion for Summary Judgment on Brown & Williamson's Counterclaims Granted; Generic Products' Motion to Dismiss Granted; that Objections to these Recommendations shall be filed within (40) days and Responses shall be filed with (20) days.

1-25-88	Defendant Brown & Williamson's Objections (Sealed) to Magistrate's Findings and Recommendations.
1-25-88	Defendant Brown & Williamson's Request for Hearing with respect to its Objections.
1-25-88	Defendant Brown & Williamson's Motion for Reconsideration of Magistrate's Findings and Recommendations.
1-25-88	Defendant Brown & Williamson's Memorandum (Sealed) in support of Motion for Reconsideration.
1-25-88	Plaintiff Liggett's Objections (Sealed) to Magistrate's Findings and Recommendations.
2-8-88	Generic Products' Response – to Magistrate's Findings and Recommendations.
2-16-88	Defendant Brown & Williamson's Memorandum of Law in Opposition to Liggett's Objections to Magistrate's Findings and Recommendations.
2-16-88	Plaintiff's Memorandum of Law in Opposition to Brown & Williamson's Motion for Reconsideration of & Objections to Magistrate's Findings and Recommendations (Sealed) filed with: Supplemental Affidavit of William H. Hogeland (Sealed).
3-7-88	Defendant Brown & Williamson's Reply Memorandum to Liggett's Opposition to Motion for Reconsideration.
3-9-88	Order of Magistrate Sharp, that Defendant Brown & Williamson's Motion for Reconsideration is Denied.

9-30-88	Order of Judge Bullock, adopting Magistrate's Findings and Recommendations as set out; trial on remaining issues will be scheduled for Spring 1989.
10-21-88	Defendant Brown & Williamson's Motion for Permission to Appeal to add to Court's Order of September 30, 1988 the statement required by 28 U. S. C. § 1292(b) to Certify Order for Interlocutory Appeal.
10-21-88	Defendant Brown & Williamson's Memorandum in Support of Motion for Permission to Appeal.
11-9-88	Plaintiff Liggett's Memorandum in Opposition to Brown & Williamson's Motion to Modify Court's Order of September 30, 1988.
3-17-89	Order of Judge Bullock, Defendant's Motion for Permission to Appeal Pursuant to 28 U. S. C. 1292(b) must be Denied.
4-7-89	Defendant Brown & Williamson's Motion to Join Grand Metropolitan, Inc. as Additional Party Plaintiff.
4-7-89	Defendant Brown & Williamson's Memorandum in Support of Motion to Join Additional Party Plaintiff filed with: Affidavit of Norwood Robinson.
4-28-89	Plaintiff Liggett's Memorandum (Sealed) in Opposition to Defendant Brown & Williamson's Motion to Join an Additional Party Plaintiff filed with: Affidavit of Josiah S. Murray, III.

5-2-89	Grand Metropolitan's Memorandum in Opposition to Defendant Brown & Williamson's Motion to Join Metropolitan as Additional Party Plaintiff filed with: Affidavit of Joel H. Gross.
5-15-89	Defendant Brown & Williamson's Reply Brief to Plaintiff Liggett's & Grand Metropolitan's Opposition to Defendant Brown & Williamson's Motion to Join Grand Metropolitan as Additional Party Plaintiff.
6-7-89	Motion Hearing & Final Pre-Trial Conference before Judge Bullock in Greensboro: Defendant's Motion to Bring Grand Metropolitan into Case Denied.
6-28-89	Defendant Brown & Williamson's Requested *Voir Dire* Questions.
7-6-89	Plaintiff Liggett's Proposed *Voir Dire* Questions.
7-7-89	Defendant's Motion to Strike Jury and Request that Case be Tried by the Court filed.

7-10-89	Jury Trial before Judge Bullock, (1st day) Defendant's Motion to Strike Jury (filed July 7, 1989) – Denied. Jury of 6 & 4 alternates Selected & Excluded until July 11, 1989, 9:30 a.m. Court directed counsel to submit jury instructions by July 27, 1989.
7-17-89	Plaintiff's Memorandum in Support of Proposed Preliminary Jury Instruct with Proposed Supplemental Instructions attached.
7-17-89	Defendant's Proposed Preliminary Antitrust Jury Instructions filed.
7-26-89	Defendant's Proposed Jury Instructions filed.
7-26-89	Plaintiff's Preliminary Proposed Jury Instructions on Liability Issues filed.
11-13-89	Defendant's Memorandum in Support of Motion for Directed Verdict dismissing Liggett's Antitrust Claim.
1-14-89	Hearing before Judge Bullock on Defendant's Motion Pursuant to Rule 50 of the Federal Rules of Civil Procedure; taken under advisement.
1-15-89	Plaintiff's Memorandum establishing its Robinson-Patman Act Claim filed.
1-30-90	Defendant's Proposed Antitrust Jury Instructions filed.
2-2-90	Jury trial resumed. (105th day) defendant rested; plaintiff made Motion for Directed Verdict as to Price Discrimination; Functional Availability; Meeting Competition; and Below

	Average Variable Costs; taken under Advisement.
2-2-90	Plaintiff's Motion for a Directed Verdict in its Favor on the Issue of Below-Average Variable-Cost Pricing filed.
2-8-90	Hearing before Judge Bullock on Charge and Document Discussion. Defendant made Motion; for Directed Verdict and plaintiff renewed Motion for Directed Verdict; both taken under advisement.
2-12-90	Hearing before Judge Bullock on Charge. Defendant's Motion for Mistrial denied.
2-23-90	Plaintiff's Proposed Jury Instructions filed in letter form.
3-2-90	Jury trial resumed. (120th day) Jury deliberations resumed at 9:00 a.m. Jury returned with verdict for plaintiff at 11:16 a.m. Plaintiff to submit Proposed Judgment and Motion on Prejudgment Interest.
3-20-90	Judgment of Judge Bullock, that Plaintiff Liggett Have & Recover of defendant Brown & Williamson sum of $148,800,000.00 which represents $49,600,000.00 trebled pursuant to 15 U. S. C. § 15(a); Plaintiff Liggett Have & Recover of defendant Brown & Williamson Post-Judgment Interest from Date of Entry of this Judgment; Plaintiff Liggett Have & Recover of defendant Brown & Williamson its Cost of Suit, including reasonable attorney's fee, amount of which shall be determined in later collateral proceeding before this Court.
4-2-90	Defendant Brown & Williamson's Motion for Judgment Notwithstanding Verdict or, in alternative, a new trial filed.

4-2-90	Defendant Brown & Williamson's Memorandum in Support of Motion for Judgment Notwithstanding, etc.
4-2-90	Defendant Brown & Williamson's Motion for New Trial Based on Trial Publicity [Sealed]
4-2-90	Defendant Brown & Williamson's Memorandum [Sealed] in Support of Motion for New Trial filed with: Affidavit [Sealed] of Ralph Simpson. Affidavit [Sealed] of Patrick Stone. Affidavit [Sealed] of Patrick Stone. Affidavit [Sealed] of Valerie Oates.
4-2-90	Plaintiff's Motion for New Trial on counts I-IV of Complaint filed.
4-2-90	Plaintiff's Memorandum in Support of Motion for New Trial, etc.
4-3-90	Plaintiff Liggett's Motion for Prejudgment Interest filed.
4-3-90	Plaintiff Liggett's Memorandum in Support of Motion for Prejudgment Interest.
4-20-90	Defendant Brown & Williamson's Memorandum in Opposition to plaintiff Liggett's Motion for New Trial on Trademark Counts (I-IV) of Co.
4-20-90	Defendant Brown & Williamson's Memorandum in response to plaintiff Liggett's Motion for Prejudgment Interest.

4-20-90	Plaintiff Liggett's Memorandum [Sealed] in Opposition to defendant Brown & Williamson's Motion for New Trial based on Trial Publicity.
4-20-90	Plaintiff Liggett's Memorandum in Opposition to defendant Brown & Williamson's Motion for Judgment Notwithstanding Verdict or for New Trial filed.
4-24-90	Motions Hearing before Judge Bullock: Defendant's for New Trial based on Trial Publicity; Defendant's for Judgment Notwithstanding Verdict or in Alternative, a New Trial; Plaintiff's for New Trial based on Trademark.
5-4-90	Plaintiff Liggett's Reply Memorandum in Support of its Motion for New Trial on Counts I-IV of Complaint.
5-4-90	Plaintiff Liggett's Reply to defendant Brown & Williamson's Memorandum in Response to Liggett's Motion for Prejudgment Interest.
5-4-90	Defendant Brown & Williamson's Reply Memorandum in Support of its Motion for Judgment Notwithstanding Verdict or for New Trial.
8-27-90	Memorandum Opinion of Judge Bullock.
8-27-90	Order & Judgment of Judge Bullock; Defendant's Motion for Judgment Notwithstanding Verdict is Granted & Jury Verdict & Judgment in favor of Plaintiff is set aside & Judgment entered for defendant; Defendant's Motion for a New Trial is Denied; Plaintiff's Motion for a New Trial is Denied.

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

DATE	FILING OR PROCEEDINGS
9-24-90	Plaintiff's Notice of Appeal filed.
9-28-90	Defendant's Notice of Appeal filed.
10-2-90	Docketing statement filed by Appellant Liggett Group Inc.
10-2-90	Disclosure statement filed by Appellant Liggett Group Inc.
10-3-90	Civil case docketed.
10-4-90	Docketing notice issued.
10-11-90	Clerk order filed consolidating case(s) 90-1851 (Liggett's main appeal) with 90-1854 (Cross-appeal by Brown & Williamson against Liggett Group, Inc.).
10-11-90	Docketing notice issued (cross-appeal).
10-15-90	Disclosure statement filed by Appellee Brown & Williamson
1-14-91	Addendum to docketing statement filed by Appellant Liggett Group Inc.
7-23-91	Page-proof cross-appeal brief filed by Appellant Liggett Group Inc.
7-25-91	Designation of appendix filed by Appellant Liggett Group Inc.
8-29-91	Page-proof cross-appeal brief filed by Appellee Brown & Williamson.
8-30-91	Designation of appendix filed by Brown & Williamson.
9-30-91	Page-proof reply brief filed by Liggett Group Inc.

9-30-91	Designation of supplemental appendix filed by appellant Liggett Group Inc.
10-10-91	Joint appendix filed.
10-16-91	Supplemental appendix filed.
10-17-91	Protective Notice of Appeal filed by Brown & Williamson (supplemental appeal).
10-18-91	Final form of cross-appeal brief filed by Appellant Liggett Group Inc.
10-18-91	Final form of reply brief filed by Appellant Liggett Group Inc.
10-22-91	Final form of cross-appeal brief filed by Brown & Williamson.
10-22-91	Final form of reply brief filed by Appellee Brown & Williamson.
10-24-91	Supplemental briefing order filed. Projected Calendar: February 1992.
10-24-91	Corrected order filed setting forth supplemental briefing and consolidating case 91-1221 (Brown & Williamson's supplemental appeal) with 90-1851 (Liggett's appeal) and 90-1854 (Brown & Williamson's cross-appeal).
10-25-91	Docketing notice issued on supplemental appeal.
10-28-91	Docketing statement filed by Appellant Brown & Williamson in its supplemental appeal.
11-4-91	Designation of appendix filed by Appellee Brown & Williamson in its supplemental appeal.
12-3-91	Supplement brief filed by Appellant Brown & Williamson.

12-3-91	Supplement appendix filed.
12-20-91	Supplemental brief filed by Appellee Liggett Group Inc.
1-3-92	Case calendared for oral argument.
2-3-92	Oral argument heard.
5-11-92	Published, authored opinion filed.
5-11-92	Judgment Order filed. Terminated on the Merits after Oral Hearing.
5-26-92	Petition filed by Appellant Liggett Group Inc. for rehearing with suggestion for rehearing *in banc*.
6-9-92	Supplemental authorities filed by Appellant Liggett Group Inc.
6-18-92	Court Order filed denying motion for rehearing and motion for suggestion for rehearing *in banc*.

UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

LIGGETT GROUP INC. Plaintiff	Civil Action No. C-84-617-D
v.	(Filed July 24, 1984)
BROWN & WILLIAMSON TOBACCO CORPORATION Defendant	

AFFIDAVIT

T. E. Sandefur, Jr., being first duly sworn, hereby states the following:

1. My name is T. E. Sandefur, Jr. I am Executive Vice President of Brown & Williamson Tobacco Corporation ("B & W"). Prior to joining B & W, I was employed by the R. J. Reynolds Tobacco Company from 1964 until 1982 in various sales and marketing positions. Because of my twenty years of direct experience in the promotion and advertising of cigarettes. I am familiar with all aspects of the marketing of cigarette products and with the highly competitive nature of the United States cigarette industry.

2. B & W manufactures and distributes KOOL, VICEROY, RALEIGH, BELAIR, BARCLAY and RICHLAND cigarettes, and non-cigarette products including SIR WALTER RALEIGH pipe tobacco and various brands of snuff, plug and chewing tobacco. B & W processes

tobacco leaf in facilities located at Wilson, North Carolina and manufactures tobacco products in North Carolina, Virginia, and Georgia.

3. B & W currently accounts for approximately 11.4% of the total cigarette market in the United States by volume of cigarettes produced. Two larger cigarette manufacturers, R. J. Reynolds Tobacco Company and Philip Morris, Inc. currently account for approximately 29.8% and 36.2% of that market respectively. The three other major cigarette manufacturers include the Plaintiff herein, Liggett Group Inc., with an approximate current market share of 5.9%, the American Tobacco Company with a current approximate market share of 8.2% and Lorillard with a current approximate market share of 8.4%.

4. Since early 1975, when B & W's market share was approximately 17.2%, B & W's market share has continually declined to its current 11.4%. To reverse this decline, B & W has over the last several years introduced several new cigarette brands such as BARCLAY, RICHLAND, FACT and ARTIC LIGHTS and has expanded its established brand lines into new market segments such as low-tars and ultra-low tars, and is currently attempting to introduce a line of generic (unbranded) cigarettes.

5. In recent years, there has been an enormous increase in the marketing of generic products. Generic products are marketed in black and white packages and the manufacturer makes no effort to create brand identity. Further, because of the use of generic packaging and the lack of advertising and other name promotion expenses, the price of generic products is less than branded, nationally advertised products with savings being passed on to

the consumer. The growth of the generic market in all areas is directly attributable to the lack of consumer concern for the point of origin or brand identification and the presence of an overwhelming concern for price. The manufacturer of generic products, in effect, represents to the consumer that the consumer is not paying for the customary advertising or other costs to promote the source of production or name. Liggett has repeatedly referred to its generic cigarettes as being "no name" and does not identify itself in any fashion on its generic cigarettes, packages or cartons as the manufacturer.

6. In 1980, total generic sales accounted for 230 million cigarettes.

7. In 1983, generic cigarettes achieved sales of over 17.5 billion cigarettes. Liggett now controls about 97% of that market.

8. Generics continue to grow. B & W expects the market to achieve sales of over 30 billion cigarettes in 1984. B & W expects the generics cigarette market to grow continually in the foreseeable future.

9. B & W's losses to generic cigarette products are disproportionately high when compared to losses by B & W's competitors. Stated another way, smokers of B & W's brands are switching to the less expensive generic products at a higher rate than smokers of competitive brands are switching to the generic products. B & W's losses to generics are about 70 percent higher than would be expected based on B & W's market share. B & W projects that by 1988, B & W's losses to generics could total 18 billion cigarettes annually.

10. In early 1984, B & W determined that it would enter the generic portion of the "economy" market.

11. B & W entered this market to regain some of the business which it had lost to generic products since 1980, to reduce any further deterioration in B & W's sales attributable to the growing generic market, and to compete effectively for a share of the market.

12. B & W is convinced that it is able to offer a highly competitive program featuring quality cigarette products that will for the first time give wholesalers and retailers the ability to choose between two competing suppliers of generics. Until now, as a practical matter, the vast majority of wholesalers and retailers who desired to purchase generic products for resale had to buy from Liggett (or from a Liggett-controlled broker/distributor network). Liggett was the sole nationwide manufacturer of such products until B & W announced its program.

13. B & W did not intend to copy any Liggett package design or trade dress. B & W was simply designing packages that would fit into the well-recognized category of generic "black and white" packaging that is found in many lines of commerce

* * *

[Handwritten Note]
[1/30/90]

UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

LIGGETT GROUP INC., Plaintiff, - against - BROWN & WILLIAMSON TOBACCO CORPORATION, Defendant.	Civil Action No. C-84-617-D

BROWN & WILLIAMSON'S
PROPOSED ANTITRUST JURY INSTRUCTIONS

Brown & Williamson submits the attached as its proposed jury instructions on the antitrust issues in this case. Brown & Williamson reserves the right to modify, withdraw or supplement these instructions.

Dated: January 30, 1990

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
By: /s/ Martin London
Martin London
Nathaniel B. Smith

- temporarily -

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Attorneys for Defendant
Brown & Williamson Tobacco
Corporation

* * *

INSTRUCTION NO. 19

In determining whether prices are predatory, you must look at what the seller reasonably believed its costs and revenues would be. Brown & Williamson's conduct would not be predatory if it reasonably believed that its revenues would be sufficient to cover its average variable costs. If you find that Brown & Williamson reasonably believed its revenues would exceed its average variable costs, you must find that it did not engage in predatory pricing. Thus, if you find that at the time it set its rebates and prices it expected to make money, then you must find that Brown & Williamson is not liable. Furthermore, if you find that Brown & Williamson reasonably believed that its costs would not exceed its revenues, but that because it had to spend unanticipated money in response to competitive activity later on after it entered the value-for-money segment its costs did exceed its revenues, then you must find for Brown & Williamson on the Robinson-Patman Act claim.

Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 233-36 (1st Cir. 1983); *MCI Communications Corp. v. AT&T*,

708 F.2d 1081, 1119-22 (7th Cir.), *cert. denied*, 464 U.S. 891, 104 S. Ct. 234, 78 L. Ed. 2d 226 (1983); *International Air Indus., Inc. v. American Excelsior Co.*, 517 F.2d 714, 723-24 (5th Cir. 1975), *cert. denied*, 424 U.S. 943, 96 S. Ct. 1411, 47 L. Ed. 2d 349 (1976); *ILC Peripherals Leasing Corp. v. IBM*, 458 F. Supp. 423, 432-34 (N.D. Cal. 1978), *aff'd*, 636 F.2d 1188 (9th Cir. 1980), *cert. denied*, 452 U.S. 972, 101 S. Ct. 3126, 69 L. Ed. 2d 983 (1981); III P. Areeda & D. Turner, *Antitrust Law*, § 715 & § 711d (1978).

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

LIGGETT GROUP, INC.,	)	
Plaintiff,	)	CIVIL NO. C-84-617-D
v.	)	
BROWN & WILLIAMSON TOBACCO CORPORATION,	)	(Filed March 2, 1990)
Defendant.	)	

ISSUES

WE, the jury in the above-entitled civil action, do answer the issues as follows:

1. Did Brown & Williamson engage in price discrimination that had a reasonable possibility of injuring competition in the cigarette market as a whole in the United States?

Yes [Handwritten]
(Yes or No)

2. If so, did Liggett Group, Inc., suffer injury to its business or property as a result of such price discrimination?

Yes [Handwritten]
(Yes or No)

3. Did Brown & Williamson engage in price discrimination in good faith with the intention to meet, but not beat, the equally low net prices of Liggett Group, Inc.?

No [Handwritten]
(Yes or No)

4. What amount of damages, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as a result of Brown & Williamson's violation of the Robinson-Patman Act?

(Do not consider this issue unless you have answered "Yes" to both Issues 1 and 2, and "No" to Issue 3.)

$49.6 million [Handwritten]
(Amount)

5. Did Brown & Williamson violate the United States Trademark Act by infringing Liggett Group, Inc.'s quality seal trademark?

No [Handwritten]
(Yes or No)

6. Did Brown & Williamson violate the North Carolina common law of trademarks by infringing Liggett Group, Inc.'s quality seal trademark?

No [Handwritten]
(Yes or No)

7. Did Brown & Williamson violate the North Carolina common law of unfair competition by infringing Liggett Group, Inc.'s quality seal trademark?

No [Handwritten]
(Yes or No)

8. Did Brown & Williamson intend to infringe Liggett Group, Inc.'s quality seal trademark?

No [Handwritten]
(Yes or No)

9. Were consumers actually confused by Brown & Williamson's infringement of Liggett Group, Inc.'s quality seal trademark?

No [Handwritten]
(Yes or No)

10. What amount, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as compensatory damages for Brown & Williamson's infringement of Liggett Group, Inc.'s quality seal trademark?

$ -0- [Handwritten]
(Amount)

11. What amount, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as punitive damages for violation of the North Carolina common law of trademarks or unfair competition?

(Do not consider this issue unless you have answered Issue 6 or 7 "Yes" and have awarded compensatory damages in Issue 10.)

$ -0- [Handwritten]
(Amount)

SO SAY WE ALL.

/s/ Rocky Alan Phillips
Foreperson of the Jury

[Handwritten]
March 2, 1990

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

LIGGETT GROUP, INC., Plaintiff,	)	CIVIL NO. C-84-617-D
v.	)	(Filed March 20, 1990)
BROWN & WILLIAMSON TOBACCO CORPORATION, Defendant.	)	

JUDGMENT

This civil action came on for trial before the court and a jury during the session of court beginning July 10, 1989, and the issues having been duly tried and answered by the jury as follows:

1. Did Brown & Williamson engage in price discrimination that had a reasonable possibility of injuring competition in the cigarette market as a whole in the United States?

Yes
(Yes or No)

2. If so, did Liggett Group, Inc., suffer injury to its business or property as a result of such price discrimination?

Yes
(Yes or No)

3. Did Brown & Williamson engage in price discrimination in good faith with the intention to meet, but not beat, the equally low net prices of Liggett Group, Inc.?

No
(Yes or No)

4. What amount of damages, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as a result of Brown & Williamson's violation of the Robinson-Patman Act?

(Do not consider this issue unless you have answered "Yes" to both Issues 1 and 2, and "No" to Issue 3.)

$49,600,000.00
(Amount)

5. Did Brown & Williamson violate the United States Trademark Act by infringing Liggett Group, Inc.'s quality seal trademark?

No
(Yes or No)

6. Did Brown & Williamson violate the North Carolina common law of trademarks by infringing Liggett Group, Inc.'s quality seal trademark?

No
(Yes or No)

7. Did Brown & Williamson violate the North Carolina common law of unfair competition by infringing Liggett Group, Inc.'s quality seal trademark?

No
(Yes or No)

8. Did Brown & Williamson intend to infringe Liggett Group, Inc.'s quality seal trademark?

No
(Yes or No)

9. Were consumers actually confused by Brown & Williamson's infringement of Liggett Group, Inc.'s quality seal trademark?

No
(Yes or No)

10. What amount, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as compensatory damages for Brown & Williamson's infringement of Liggett Group, Inc.'s quality seal trademark?

$0.00
(Amount)

11. What amount, if any, is Liggett Group, Inc., entitled to recover from Brown & Williamson as punitive damages for violation of the North Carolina common law of trademarks or unfair competition?

(Do not consider this issue unless you have answered Issue 6 or 7 "Yes" and have awarded compensatory damages in Issue 10.)

$_____
(Amount)

NOW, THEREFORE, IT IS ORDERED AND ADJUDGED that Plaintiff Liggett Group, Inc., have and recover of Defendant Brown & Williamson Tobacco Corporation the sum of ONE HUNDRED FORTY-EIGHT MILLION EIGHT HUNDRED THOUSAND DOLLARS

($148,800,000.00), which represents Forty-Nine Million Six Hundred Thousand ($49,600,000.00) trebled pursuant to 15 U.S.C. § 15(a); and

IT IS FURTHER ORDERED AND ADJUDGED that Plaintiff Liggett Group, Inc., have and recover of Defendant Brown & Williamson Tobacco Corporation post-judgment interest from the date of entry of this judgment, as provided by law under 28 U.S.C. § 1961(a); and

IT IS FURTHER ORDERED AND ADJUDGED that Plaintiff Liggett Group, Inc., have and recover of Defendant Brown & Williamson Tobacco Corporation its cost of suit, including a reasonable attorney's fee, as provided by law under 15 U.S.C. § 15(a), the amount of which shall be determined in a later collateral proceeding before this court.

/s/ Frank W. Bullock, Jr.
United States District Judge

[Handwritten]
March 20, 1990

IN THE UNITED STATES DISTRICT COURT
FOR THE MIDDLE DISTRICT OF NORTH CAROLINA
DURHAM DIVISION

LIGGETT GROUP, INC.,	)	
Plaintiff,	)	CIVIL NO. C-84-617-D
v.	)	(Filed Aug 27, 1990)
BROWN & WILLIAMSON TOBACCO CORPORATION,	)	
Defendant.	)	

ORDER and JUDGMENT

BULLOCK, District Judge

For the reasons set forth in a memorandum opinion filed contemporaneously herewith,

IT IS ORDERED AND ADJUDGED that Defendant's motion for judgment notwithstanding the verdict pursuant to Rule 50(b), Federal Rules of Civil Procedure, be, and the same hereby is, **GRANTED,** and that the jury verdict and judgment in favor of the Plaintiff be, and the same hereby is **SET ASIDE,** and judgment entered for the Defendant; and

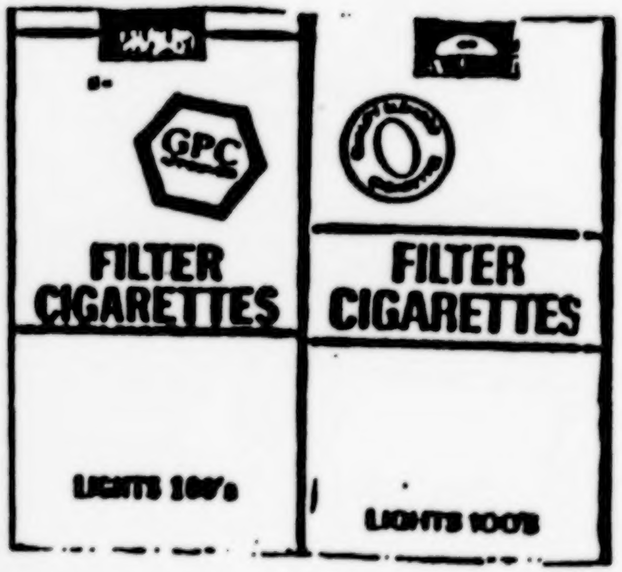
IT IS FURTHER ORDERED that Defendant's alternative motion for a new trial pursuant to Rule 59, Federal Rules of Civil Procedure, be, and the same hereby is, **DENIED;** and

IT IS FURTHER ORDERED that Plaintiff's motion for a new trial pursuant to Rule 59, Federal Rules of Civil Procedure, be, and the same hereby is, **DENIED.**

/s/ Frank W. Bullock
United States District Judge

[Handwritten]
August 27, 1990

Theirs Ours



Theirs Ours

Theirs Ours

Theirs Ours

[Illegible]

A.L. (AL) Cagney
National Sales Manager
Private Label and Generics

August 11, 1981

TO: Jim Dowd

FROM: Al Cagney

SUBJECT: FRANCHISE DISTRIBUTION REPORT
NSM-053

A month or so ago a letter was sent to all Generic Region Managers with a request for their feedback and recommendations pertaining to the above subject class of Gary Tobacco sales.

Please find attached copies of those reports submitted by the Region Managers.

Summarizing the results of their reports is a vast task. You will note that some managers state that ineffective and distributors [sic], with little interest should be dropped immediately from the program. Other managers state lets see what happens during the 3rd and present calendar quarter before making any decisions.

In summary, I recommend the following:

1. During the month of September a final decision be made regarding the Franchise Distributor Program which would be effective *October 1, 1981*.
2. That the accounts that don't have the correct type of retail outlets (large carton type outlets), and/or the correct attitude be dropped from the program. The accounts to be dropped will be given the option of switching to G.P.C. or Class A. Notified in writing.

3. The firms that remain on the program will:

   A. Will receive a rebate payment of $3.00 per case for all purchases over 100 cases for said quarter. $6.00 per case for all purchases over 250 cases and $7.80 per case for all purchases over 500 cases.

   B. That Gary Tobacco Company supply *Free* all display and point of sale material to distributors that sell a minimum of 250 cases per quarter.

   C. Minimum Shipments be dropped from 25 cases to 15 cases delivery point, and the order department is to see that this followed. And only the authorized accounts can purchase these brands.

I realize that some of these recommendations seem harsh and favor the larger more successful distributor, but that is my intent.

Thank you.

/s/ [Illegible]
AJC:ca

Attachment

COMPETITIVE POSSIBILITIES:
RESPONSES AND LIABILITIES
GENERIC/PRIVATE LABEL CIGARETTES

April 23, 1982

* * *

MAJOR TOBACCO COMPANY ENTERS MARKET:

<u>RESPONSE LIABILITIES</u>

DEVELOP BRAND FOR DISTRIBUTOR TRADE (I.C.C.)
- UTILIZE L&M SALES FORCE
  - NO DIRECT COST EFFECTS
  - LOWER PRODUCTIVITY ON NATIONAL BRANDS
- INSTITUTE "GUARANTEED" SALE "TEST"
  - OFFER PROGRAM ONLY TO DISTRIBUTOR TRADE AS A "TEST"
  - GUARANTEED SALE
  - ESTIMATED 2½% RETURNED GOODS.
    1983 VOLUME ESTIMATE = 547,200M UNITS
  - LIABILITY FOR 2½% RETURNS = 13,680M
  - ESTIMATED LIABILITY: $95,760
- INCREASE EXISTING REBATE
  - CURRENTLY OFFERING $6 PER CASE REBATE QUARTERLY TO ALL DISTRIBUTORS
  - INCREASE TO $9 PER CASE QUARTERLY FOR ALL
  - SUPPLEMENT ADDITIONAL $5 PER CASE FOR THOSE WHO SELL OVER 500 CASES QUARTERLY
  - ESTIMATED ADDITIONAL LIABILITY, BASED ON 1983 VOLUME ESTIMATE: $260,400

B & W
[LOGO]

BROWN & WILLIAMSON TOBACCO CORPORATION

DOMESTIC COMPETITIVE ANALYSIS

1983 UPDATE

RESTRICTED MAY 1983

* * *

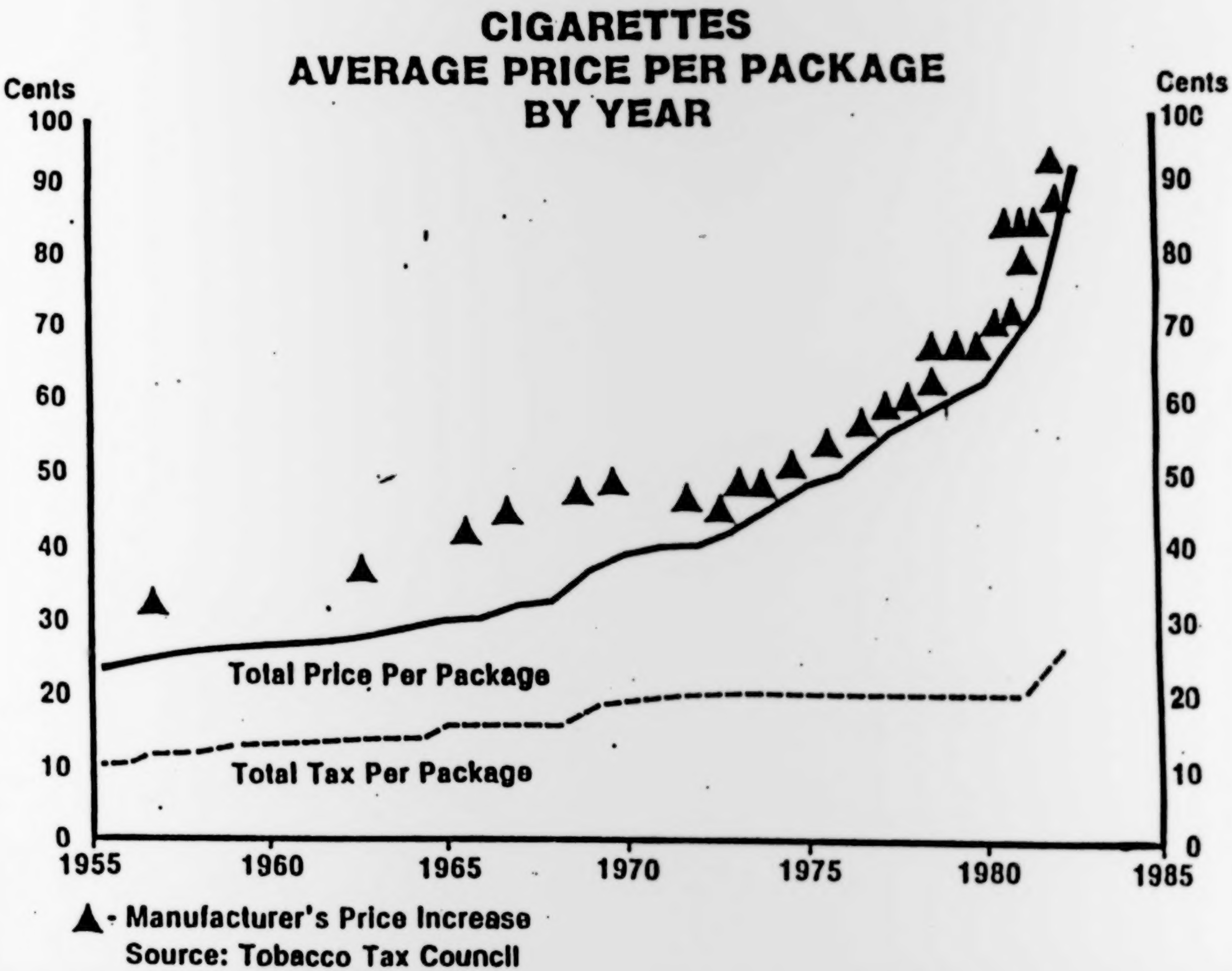
Liggett & Myers

1. *L&M will do whatever possible to increase generic distribution and sales.*
   - L&M is estimated to begin trying to contract for generic sales through increased types of retail outlets, seek longer-term generic sales contracts, if possible, develop private label long-term contracts, etc.

   - L&M has very little branded business to lose, so it will attempt to transfer new ideas to generics, as long as the business can be profitable for them.

[August 8, 1983]

CHART 11



[August 8, 1983]

CHART 12

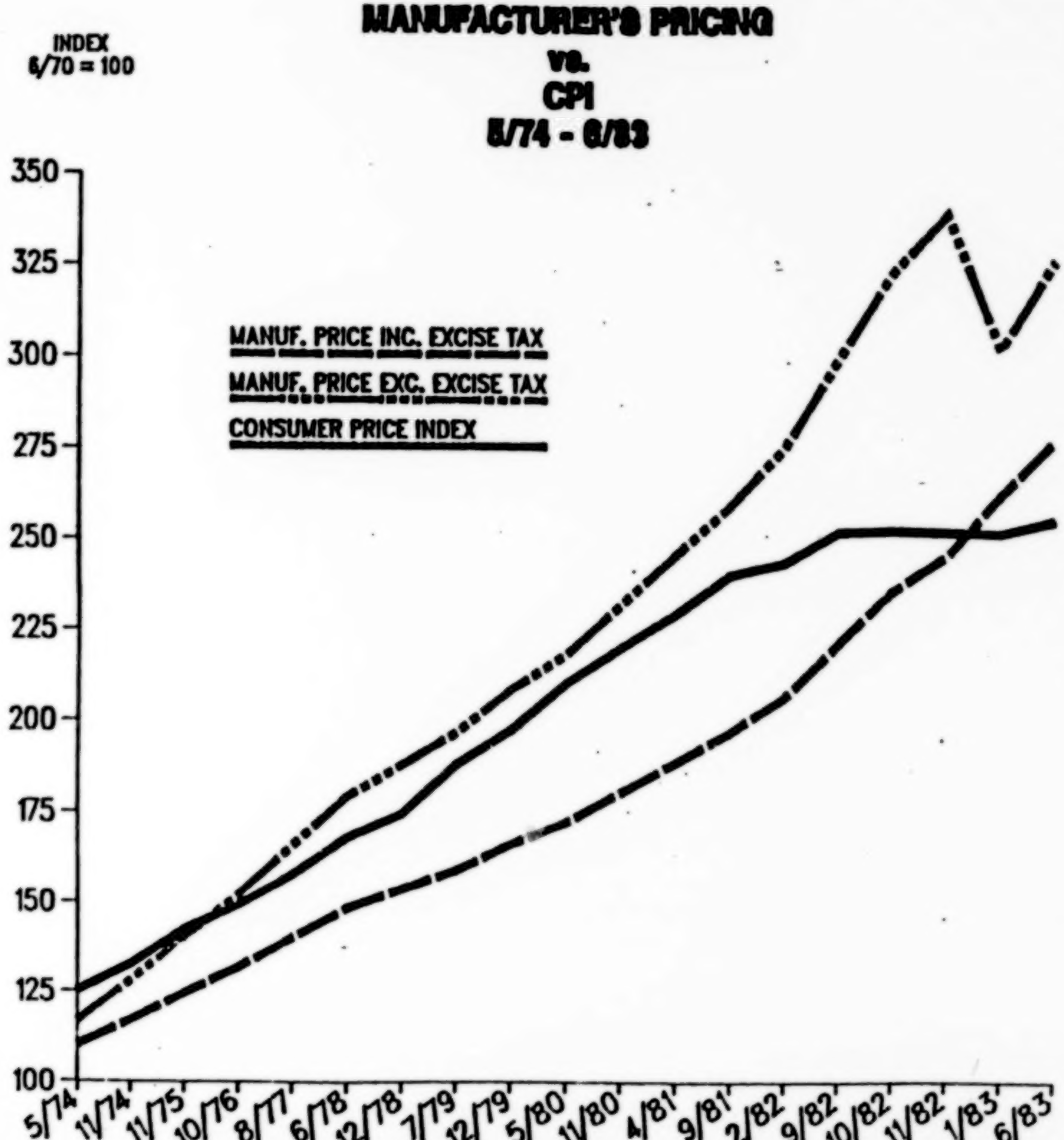
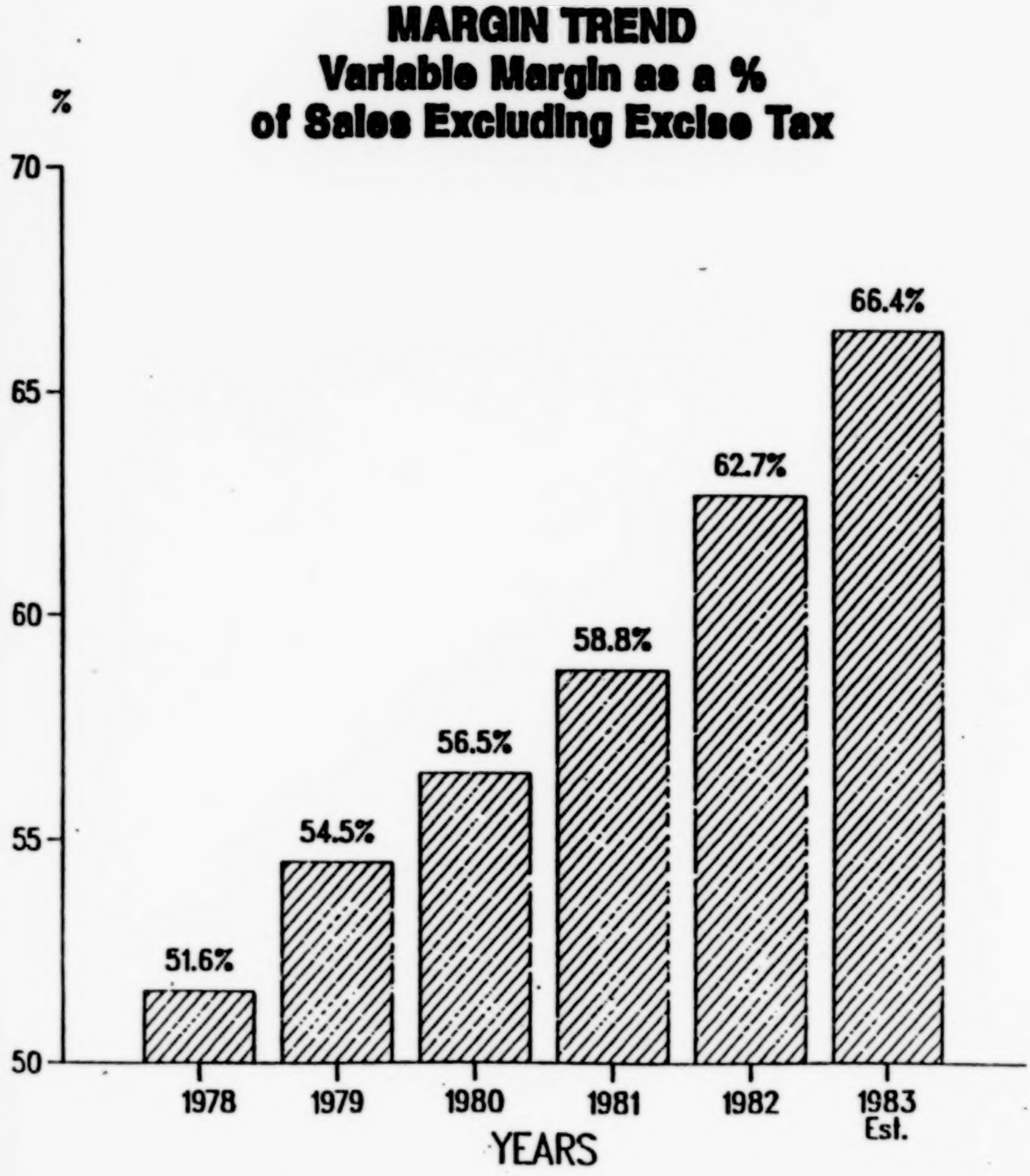


CHART 13 [August 8, 1983]



GARY TOBACCO COMPANY
STRATEGIC PLANNING

AUGUST 31, 1983

* * *

II. *ENVIRONMENTAL ANALYSIS*

A. COMPETITION
- CURRENT COMPETITION (U.S. TOBACCO) NOT TO BE CONSIDERED A FACTOR IN LONG-TERM PLANNING
- POTENTIAL MAJOR COMPETITION
  - COMPETITIVE TIMETABLE FOR ENTRY, ADVANCED (DUE TO EXCISE TAX SUCCESS)
  - ACCELERATED PLANNING ANTICIPATED
  - MID-PRICED ENTRY PROBABLY (REFERENCE MAXWELL REPORT, EUROPEAN SITUATION)
  - VALUE ADDED OR 25 PACKS

B. SITUATION
- GENERIC/PRIVATE LABEL CONSUMER GOODS CATEGORY FLAT TO DECLINING
- U.S. ECONOMY APPEARS TO BE STRENGTHENING, I.E., INFLATION RATE HAS SLOWED
- CONTINUED STATE TAX INCREASES AND POTENTIAL FEDERAL TAX INCREASES ANTICIPATED

- SHORT-TERM ENVIRONMENT CONTINUES TO BE FERTILE; LONG-TERM UNPREDICTABLE
- INDUSTRY PRICE INCREASES EXPECTED TO BE LESS FREQUENT AND/OR NOT AT SAME LEVEL AS HISTORICAL INCREASES (% INCREASES WILL DECLINE)

* * *

LIMITED

BROWN & WILLIAMSON TOBACCO CORPORATION

INTERNAL CORRESPONDENCE

E.E.K.

JAN 25 1984

TO	D.S. Johnston	H.A. Roeder	E.E. Kohnhorst
DEPT.	C.J. Dunn	C.J. Heger	R.H. Sachs
C.C.to			
"			
"			

FROM E. T. Parrack, Jr. DATE January 25, 1984
SUBJECT Generics Work In Progress

PURPOSE

1. To provide background information on our analysis of Generics and

2. To request your help in locking up a timetable for launch.

[ILLEGIBLE]

1. Background draft document attached. Many numbers are still rough, subject to validation. Overall thrust is reflective of our thinking to date. E.G.:

   a. Generics are growing: +0.1 SOM/month

   b. L&M represents 97% of segment

   c. Business is mixed between (*numerous*) white and private lable styles

d. Volume can be gained by offering a superior net price (same basic list) as L&M and superior customer service. (Service to be tailored by customer needs/sensitivities.)

2. We need your help on various timetable issues:

R&D/Man/Finance

a. Blend specification and standard costs

1) R&M Lights Kings, 100's

2) R&M Ultra Kings

3) R&M full taste

4) R 70mm plains

* * *

* * *

CURRENT	BACKGROUND
PRODUCT CAN BE SHIPPED WITH OTHER L&M BRANDS TO MEET MINIMUM SHIPPING REQUIREMENTS TO ACCOUNTS	• HELPS L&M MAINTAIN DISTRIBUTION ON MARGINAL BRANDS

B. PRICE

17.25 PER M

2% DISCOUNT 10 DAYS NET

TARGET PER QTR.	VOLUME DISC.	"GROWTH" DISC.
2,000 CS.	5¢/CTN.	15¢/CTN.
1,000 CS.	3¢/CTN.	13¢/CTN.
250-1,000 CS.	1¢/CTN.	11$/CTN.

VOLUME DISCOUNT FROM 0-5¢ (1983) 8,000 CASES/YR. = 5¢/CTN. 4,000 CASES/YR. = 1¢/CTN.	VOLUME OR PROMOTION DISCOUNTS OFF INVOICE AND THROUGH REBATES
GROWTH DISCOUNT UP TO 20¢/CTN. REBATE ON VOLUME OVER AND ABOVE LAST YEAR'S SALES	ALL CONTRACTS DRAWN BY GARY TOBACCO
ADVERTISING DISCOUNT UP TO 12¢/CTN. FOR 60-90 DAYS (OCT.-DEC. 1983)	RETAIL CHAIN/ WHOLESALER PAYS GARY TOBACCO FOR AD AND RECEIVES BETTER RATES
DISPLAY FIXTURE ALLOWANCE VARIES FROM CHAIN PURCHASE AND OWNERSHIP TO FREE FIXTURES	NO AUTHORIZED PAYMENTS BY GARY TOBACCO FOR DISPLAYS
NO RETURNED GOODS – ALL SALES FINAL	

THE REAL PRICE OF GENERICS TO MAJOR ACCOUNTS IS DISGUISED BY THE VARIOUS DISCOUNT SCHEMES AND ALLOWANCES. THEY HAVE USED PRICE AS THEIR KEY STRATEGY FOR GROWTH. NO PRICE INCREASES PLUS INCREMENTAL VOLUME DISCOUNTS.

PRICING*

MANUFACTURER'S PRICE (PER THOUSAND)

(LIST - DISCOUNT)

B&W : 28.20

$11.51 SPREAD

GENERIC: 16.69

↓

DIRECT ACCOUNT PRICE

(INCLUDES STATE TAX)

B&W : 38.58

$10.33 SPREAD

GENERIC: 28.25

↓

RETAIL ACCOUNT PRICE →	TO CONSUMER:
	(PER CARTON)
B&W : 42.25	8.45
$9.35 SPREAD	1.87/CTN. SPREAD
GENERIC: 32.90	6.58

*MAJOR VARIANCES OCCUR AT EACH POINT BELOW MFG LIST DUE TO:

- STATE/CITY TAXES
- DIRECT ACCOUNT VOLUME DISCOUNTS TO CHAINS
- CHAIN PRICING STRATEGY

* * *

/LR/522T

OBJECTIVE	STRATEGY	FOCUS

A. VOLUME
6 BILLION UNITS DURING FIRST YEAR

1. DEFINE TARGET CUSTOMERS. IDENTIFY THE MAJOR ACCOUNTS WHICH B&W MUST ACQUIRE IN ORDER TO ACHIEVE VOLUME
2. ACHIEVE MAXIMUM DESIRED VOLUME THROUGH A MINIMUM NUMBER OF CUSTOMERS. THIS ALLOWS FOR COST EFFICIENCIES AND TAILORING OF THE OFFER TO MAKE IT UNIQUE, SUPERIOR (TO COMPETITION) AND MORE DIFFICULT TO MATCH. CREATE A PROGRAM MIX FLEXIBLE ENOUGH TO PROVIDE CUSTOMERS SATISFACTION AT MINIMUM COST.
3. DEFINE THE KEY SELLING – LEVERAGE POINTS OF EACH ONE OF OUR LARGEST VOLUME ACCOUNTS.
   - DETERMINE TOTAL COSTS B&W IS WILLING TO INCUR BASED ON VOLUME FOR EACH CUSTOMER
   - MATCH CUSTOMER NEEDS TO PROGRAM OFFER

THE EFFECT OF SUCCESSFULLY PURSUING THIS STRATEGY IS TO DEVELOP AND MAINTAIN

– MARKET SEGMENTS BY VOLUME

I. MILITARY
   A. OVER 2 BILLION UNITS
   B. SEGMENTS
      – COMMISSARIES
      – EXCHANGES

TYPE	# BUYING OFFICES	% VOLUME (B&W) (OF MILITARY & INST.)
AIR FORCE COMM.	172	47.36
ARMY COMM.		28.76
ARMY & AIR FORCE EXC.	6	14.24
NAVY EXC.	68	10.95
MARINE EXC.	30	2.42
COAST GUARD EXC.	18	2.33

   C. GENERIC SHARE GROWTH (EST.) 10-12% OF MILITARY CIGARETTE BUSINESS AND GROWING

MILITARY – 1982-1983

1ST QTR '82	2ND QTR '82	3RD QTR '82	4TH QTR '82	1ST QTR '83	3RD QTR '83
2.6	3.09	3.76	4.59	6.16	7.84

Lehman Brothers Research

Industry Comment

The Maxwell Report
Revised 1983 Year-end Sales Estimates for the Cigarette Industry

John C. Maxwell, Jr.
(202)558-2287 February 2, 1984
LEHMAN BROTHERS KUHN LOEB INCORPORATED
55 WATER STREET, NEW YORK, NEW YORK 10041
(212) 558-1500

THE MAXWELL REPORT

It Was A Difficult Year

The cigarette industry's 1983 volume was on target with our preliminary figures. In October we estimated total consumption at 596.59 billion units; the actual number was 596.19 billion, down 4.5% from 1982.

We believe that 1984 will be another difficult year, and we are not sanguine about much of an uptick. Taxes were increased by 14 states in 1983, preponderantly in the latter part of the year, with boosts averaging $0.06. This year at least 10 more states are expected to increase taxes. On average, taxes now account for 37% of retail cigarette prices. An average pack on November 1, 1983 (before the latest price hike) cost $0.95. Thus, there is the possibility that industry numbers could be flat or down in 1984 and beyond.

Generics are now running at an annual rate of 3.5% of the market against 2.9% for 1983, and we suspect that generics' 1984 share will be in the 3.5%-4% area. The industry can no longer neglect this growing sector, and there could be two attacks in this area. The first is obvious – other companies could introduce generics. The second would be for some smaller companies to reintroduce a few of their tired brands as discount products. We suggest that products that have used coupons in the past might be among the first out. If this were to take place, we would expect responses from larger companies, which could introduce new brands to compete in the discount sector. We would not be surprised to see this type of situation transpire in the next six months.

At press time, R.J. Reynolds had just announced plans to run a series of ads to put the health issue into better perspective. This is the first time the industry has publicly defended itself against the health activists, and we think it is a constructive move.

Our other comments in the October 25, 1983 Maxwell Report remain intact.

MEMORANDUM LIMITED

TO: MR. C. J. HEGER
[Crossed out]

FROM: MR. A. C. DIEBOLD

DATE: FEBRUARY 7, 1984

SUBJECT: GENERIC BUSINESS

At your request, I have roughed out the potential loss which would accrue to B&W assuming we would manufacture and sell 18 billion units of Generics at a breakeven point at the variable margin level. The results of my calculations are given below.

	Annual Loss $000
A. Loss in interest income of funds tied up in working capital related to Generics (calculated at 12% of roughly $120 million).	$ 14,400
B. Approximate cost (loss) of incremental overheads (Macon Branch at 40¢ per M)	7,200
C. Estimated cost (loss) of marketing and selling field and/or broker's fees at 60¢ per M	10,800
Total in terms of current dollars	$ 32,400

Sensitivities regarding "Target" value will be developed shortly.

/s/ A. C. Diebold
A. C. D.

/sr

GENERICS PRESENTATION

FEBRUARY 9, 1984

* * *

SITUATION ANALYSIS

1. L&M *IS* THE GENERIC SEGMENT AND B&W *IS* A MAJOR CONTRIBUTOR TO ITS GROWTH.

L&M ENTRY:

1983 • 97% OF TOTAL GENERIC SEGMENT

1983 • 3.77% OF INDUSTRY VOLUME (NOVEMBER 1983)

1983 • +16 BILLION UNITS ANNUALLY

1984 • .083 SHARE POINTS PER MONTH (PROJECTED) GROWTH RATE

1984 • 24 BILLION UNITS (PROJECTED)

B&W CONTRIBUTION:

1982 • 4.9% OF B&W'S LOSSES WERE ATTRIBUTED TO GENERICS (MAY 1982 SWITCHING STUDY)

1983 • 14.2% OF B&W'S LOSSES WERE ATTRIBUTED TO GENERICS (MAY 1983 SWITCHING STUDY)

1983 • 23% OF GENERIC GAINS WERE (FORMER) B&W SMOKERS (MAY 1983 SWITCHING STUDY)

* * *

GENERICS

OBJECTIVE:

TO DEVELOP AND EXECUTE A PROGRAM WHICH WILL DELIVER VOLUME YEAR ONE OF SIX BILLION CIGARETTES

CONSTRAINTS:

1. DO NOT ACCELERATE SEGMENT GROWTH
2. DO NOT ACCELERATE GENERIC EROSION OF B&W EXISTING BUSINESS
3. AVOID/MINIMIZE DIVERSION OF B&W RESOURCES
    - HUMAN
    - FINANCIAL
    - MANUFACTURING

General Products Strategy

Acquire 6 billion sticks in 1984 by:

1. Offering white label
   private label
   products comparable to L&M's
   to all trade customers
2. Offer superior net costs to L&M
   - A. Same list price
   - B. Superior
     1) Volume discount (front loaded credit for stock)
     2) Growth discount
     3) Merchandising allowances
     4) Fixture allowance

– Stratified by customer volume

3. For Military:

   Offer superior price for a branded generic

* * *

- . . . WHY NOT STRAIGHT PRICE COMPETITION?
- REDUCING THE LIST PRICE TO DIRECT ACCOUNTS WOULD:

↓

- ENCOURAGE SUPPLIERS TO REDUCE THEIR SELLING PRICE TO RETAILERS.

↓

- ENCOURAGE RETAILERS TO PASS ALONG THESES SAVINGS TO CONSUMERS AND STIMULATE USE OF GENERIC CIGARETTES AS A LOSS "LEADER."

↓

- WIDEN THE PRICE DIFFERENCE BETWEEN GENERICS AND BRANDED CIGARETTES

↓

- MAKE MORE SMOKERS RECEPTIVE TO "PRICE VS. IMAGE" TRADE OFF.

↓

- ACCELERATE SEGMENT GROWTH.

↓

- CONTINUE AND INCREASE RATE OF EROSION ON B&W BRANDS TO GENERICS.

↓

- FORCE ACTION BY L&M AND OTHER MANUFACTURERS.

↓

- FURTHER EXPLODE CATEGORY.

↓

- FURTHER REDUCE PROFITABILITY.

* * *

HOW DO WE GET THE BUSINESS

1. Equal or better L&M's offer by customer.
2. Generate target volume from minimum number of customers.

PROGRAM

1. Match L&M list price.
2. Offer discounts (per carton) to:

   5 levels – Domestic

   (Military Separate)
3. Structure terms and discounts based on volume and exclusivity.

DOMESTIC VOLUME LEVELS

LEVEL	VOLUME (CASES PER YEAR)
1	OVER 25,000
2	12,000 – 24,999
3	6,000 – 11,999
4	3,000 – 5,999
5	1,000 – 2,999

[Approximate Date:
1st quarter 1984.
See Tr. 23:106,112]

[Handwritten Notes]

Short Term –
Long Term – a) maint. Seg. [Illegible]
b) [Illegible] Segment [Illegible]
c) limit potential for competitive [Illegible] & response

Sub Head (Implications)

Assume --- (from prev. page)
of monthly volume flow chart

---

strategy –

Investment strategy

two tiered
[utilize full net VM to obtain business 1984

Volume generation strategy, obtain vol from top cust.
Implication – show deal to customers.

Match L&M List under L&M in Military use discounts

↓

Superior offer in simplified form.

Distribution

Volume Levels

Military

Product

Start by Matching styles – not specs – closer in net delivery to L&M's product –

Packaging –

break out white label vs. private label

"Make it look like theirs" – for all customers – minimize visible difference in product offerings

– do we go directly after GPC contract

- – Primary call
- – Leveraged call

RJR intensify coupons:

PM – Continue/intensify sampling
– enter coupon
– tape on
When loss rate to generics exceeds RJR SOM drops below #1

If B&W not in

Someone else will PM/RJR sooner if we don't go in.

Someone must put a lid on L&M – if we do – does someone else need to??

No reason to increase spread – no proof that it will increase volume financial impact of growth of generics on VM – what is it worth to defend volume

RJR/PM "branded generic" side

Signal intent to competition – not expand segment protecting ourselves – get back what we lost.

Profile of LOK ACC cost of goods.

[Illegible] incremental bus. if can get in efficiently

– reducing dependence on cigarettes

RJR PM – tobacco philosophy & orientation

[Approximate Date:
1st Quarter 1984.
See Tr. 47: 196]

GENERIC CIGARETTE CATEGORY

* * *

To compete head to head with Liggett on the price frontier would be a very risky business. They have already demonstrated restraint in raising generic prices, moreover, faced with competition it is believed they would not hesitate to lower prices. The generic category *is* L&M. Any threat to generics is a threat to their existence. If the wholesalers and chains believe that a new entry at a reduced price will merely serve to drive down the price of their current generics, they will not replace the system they already have in place. Moreover, there is little reason to believe that they will carry similar discounted brands manufactured by two companies. Product differentiation must be apparent.

PLACE

We learned from Liggett's history that:

1. Generic strength *is* regional in nature (as is generic weakness).
2. Distribution is essential in chains, supermarkets and distributors.

The cause of the regional variability in share development is not singular and needs further study from two perspectives:

1. Why do generics sell (in some areas)?
2. Why *don't* generics sell (in other areas)?

For B&W, these answers are prerequisites of plans for any roll out, creation of an image, and an overall better understanding of what is driving the category.

If a B&W entry into the category could replace the Liggett brands in distribution (versus competing side by side), then the category would be ours. The key then is to offer a better overall program to wholesalers than Liggett currently offers and superior to *whatever* Liggett is capable of producing. Matching their program and touting a superior product and/or sales effort may not be enough to dislodge their monopoly of the distribution channels.

PROMOTION

Promotion pays out when:

1. It leads to heightened positive awareness which leads to trial and repeat purchases (to date, it is difficult to say that many smokers have really *converted* to generics).
2. It causes better in-store visibility and availability to the same end (i.e., repeat purchases).

Liggett's promotion through co-op advertising and fixtures does this better than most promotion efforts because they have been able to emphasize the price spread between generics and 20's, demand quantity purchases (which reduces out-of-stocks) and have attained prime display space to insure visibility. Furthermore, the chains and distributors have a "vested interest" in the

product due to stock investments, no returns and higher margins.

Successful competition in the category almost requires displacing Liggett's position at retail and with wholesalers and chains to obtain the necessary support. Liggett's message is clearly quality and value. While their quality has not been perceived as commensurate with branded products, it's value due to price has. Another entry singing the same song may need more apparent evidence of superior quality and value to distinguish itself from generics.

SUMMARY

A product designated to successfully compete in Liggett's generic category must be able to:

1. Dislodge a large portion of the current and future L&M generic and private label smokers.
2. Develop a permanent, loyal franchise that does not whither [sic] with an improved economy.
3. Satisfy the chain and distributor needs so as to create the same kind of "vested interest" that Liggett has achieved which will insure acceptance, participation, and product availability.

In essence, *beat their deal*. But it must be done in a way that cannot easily be duplicated.

[February 1984.
See Tr. 9:103, 106]

SITUATION ANALYSIS

I. *Background*

Generic cigarettes currently have over 3.5% of the total U.S. cigarette business. No one in the industry – including Liggett and Myers – anticipated this rapid growth and widespread acceptance.

To position B&W's generic program, the following subjects have been analyzed:

- The market for generic products in general.
- The market for generic cigarettes
  - generic cigarettes versus generic products
  - generic cigarettes versus branded
- L&M: A historical review of their success.
- Additional "Value for Money" options to explore.

A. *Generic Product Development*

Generic products have developed over the past five years driven by changing social trends, lifestyles and values.

The 1983 Yankelovich Monitor of social trends reports that consumers are shifting at an increasing rate away from the following attitudes, values and lifestyles:

1. Immediate gratification (Hedonism)
2. Belief that "qualify life" will always improve in the U.S.

3. Dependance on physical attributes and brand name possessions to portray self worth

These changes create potential for generics: some consumers are willing to sacrifice brand names for a lower price. They realize that a certain portion of a product's selling price results from the advertising and promotion costs of image presentation (versus real product difference). From these realizations, new values are forming: some consumers believe they can distinguish quality without depending on reassurance of brand name (self reliance).

* * *

B. *L&M Generic Strategies*

L&M's rapid development in the generic segment has resulted from a number of key strategic decisions. These include:

1. *Taking advantage of marketplace dynamics by widening the price differential between branded cigarettes and generics.*

   When L&M chose not to raise prices during the general price increase in December, 1982, July, 1983, and again in December, 1983, at which time the federal excise tax was doubled, share gains were immediate and dramatic.

Manufacturing Net Selling Price

	Jan. 1983	July 1983	Jan. 1984
Branded			
Kings	$ 26.03	$ 27.48	$ 28.20
100's	$ 26.99	$ 28.44	$ 29.17
Generics			
Kings	$ 16.90	$ 16.90	$ 16.90
100's	$ 17.89	$ 17.89	$ 17.89

Margin Spread – Branded vs. Generic

	Jan. 1983	July 1983	jan. 1984
Dollars			
Kings	$ 9.13	$ 10.58	$ 11.30
100's	$ 9.10	$ 10.55	$ 11.28
Percent			
Kings	35.0%	38.5%	40.0%
100's	33.7%	38.4%	38.7%

The result of this strategy was that more consumers were willing to make the tradeoff as branded cigarettes shifted to a more price elastic position on the demand curve.

* * *

Brown & Williamson Generic Objectives

Year 1 — *Became a dominant factor in the generic market, targeting for at least a 60% share of the generic market at end of Year 1.*

Given that the Company cannot be certain how quickly volume will be established, we project that volume falling into 1984 will be between 3.7 and 6.0 billion sticks (detailed in the financial section).

Outyears — *Maintain dominance of the generic market (at least a 60% share of the generic market).*

Other key long-term objectives are to:

- Manage segment growth
- Limit potential for competitive entries by minimizing profit capability

- Minimize generic erosion of B&W existing business
- Minimize diversion of B&W resources
  - Human
  - Financial
  - Manufacturing

These objectives will be achieved while other full major margin brands are being developed for marketplace implementation.

Brown & Williamson Generic Strategies and Tactics

I. *Investment Strategy*

B&W's generic investment strategy is to spend up to net variable margin in order to achieve share objectives ($2.67/M).

This spending strategy will provide customer support advantages versus L&M. In the event that L&M decreases their price, B&W's contingency plans are to have a "cushion" in cost per thousand which will allow B&W to match L&M's offer down to full variable margin ($3.17/M if necessary); however, we would not go below full variable margin to a point where we would be losing money.

In addition, B&W plans to customize support so it is most responsive to customer needs (in essence, not vary total support on a carton basis among similar volume accounts, but possibly vary how the money is spent).

II. *Volume Generation Strategy*

Required volume will be achieved by going to the minimum number of major customers necessary.

This is the most cost efficient and effective means of gaining generic dominance in the shortest period of time.

Further, the Company will work to obtain a share of key account generic volume still under contract with L&M targeting to become the sole supplier when contracts come up for renewal.

III. *Product Strategy and Tactics*

B&W's overall product strategy for generics is to offer high quality cigarette products which are similar in product acceptance to current generics.

In addition, we plan to offer a by-style line-up similar to current generics.

The basis for this product strategy is that comparability will limit consumer acceptance issues. Comparable products will also ease trade sell-in.

Our product line-up is recommended as follows:

* * *

IV. *Pricing and Bonus Payments Strategy and Tactics*

B&W's generic pricing strategy is to match the L&M list price but make the B&W total offer more attractive by offering greater bonus payments.

The rationale for this strategy is that it will place B&W in an advantageous position to sell-in our offerings, but will not tend to make the segment more attractive to other cigarette companies. For perspective, if B&W reduced the list price to accounts, it might lead to the following unacceptable scenario:

- Reducing the list price to direct accounts would:
- Encourage suppliers to reduce their selling price to retailers.

- Encourage retailers to pass along these savings to consumers and stimulate use of generic cigarettes as a loss "leader."
- Widen the price difference between generics and branded cigarettes.
- Make more smokers receptive to "price vs. image" trade off.
- Accelerate segment growth.
- Continue and increase rate of erosion on B&W brands to generics.
- Force action by L&M and other manufacturers.
- Further explode category.
- Further reduce profitability.

In the B&W program, discounts per carton will be offered at five different volume levels. Terms and discounts will be structured to be based on volume and exclusivity.

B&W's bonus program will consist of the following major elements:

* * *

FINANCIAL

GENERIC LONG TERM PRICING STRATEGY

B&W's long term pricing strategy is as follows:

- Manage the category growth by preventing an increase in the *percent* pricing spread between generics and branded cigarettes. This will be accomplished via one of the following tactics, depending upon the environment at the time of price increases:

  - Maintain a constant percent margin difference (at 40%) between the prices (Schedule I)
  - Allow the percent difference to decrease by maintaining a constant dollar spread (Schedule III)
- Maintain a fixed dollar amount of *contractual* trade allowances for direct buying customers and non-direct chain accounts.
- Build in "contingency reserve" of dollars which can be used to maintain dominance of the segment and combat competitive entry.

The strategies for pricing were developed based upon the need to determine a list price which will be consistant [sic] with B&W's major objectives of:

- Generating volume
- Dominating the category
- Managing the category growth
- Minimizing opportunities for competitive response

This requires consideration of both list price and trade allowances over the next five years according to the estimated price increases on B&W's branded product lines.

Three schedules are attached which show how various changes in list price and/or trade allowances would affect B&W trading profit. Schedule IV is provided as an indication of how a mid-point price would compare to branded product and generic product pricing over time.

Further explanation is as follows:

1. Schedule I maintains a generic price increase which is 60% of the expected increase on B&W branded cigarettes.

   Although this will increase the *dollar* spread between generics and branded, the *percent* difference remains constant. Consumers will not have increased motivation to trade-off image for price as *has been* the case with L&M not increasing their prices on generics when branded product prices increased.

   Schedule I also maintains trade allowances over time at an average of $1.65 per thousand. This serves to discourage passing along incremental allowances to the retailers and consumers, which would further expand the category.

   Schedule II, which is not recommended, shows the bottom line results under a similar pricing scenario, but where B&W retains only a portion of each price increase to cover incremental costs and passes along the balance to the trade in the form of increased allowances.

2. Schedule III presents another viable tactical approach to our pricing strategy. Instead of maintaining a *constant* percent margin difference between generics and branded, this strategy maintains a constant dollar spread which *decreases* the *percent* difference. This allows us the flexibility needed to resond [sic] quickly to the competition by using short term trade allowances which are not bound by contracts or extended time frames. For example, B&W could offer an extension of (up to) three months at the old price when prices increase on generics.

* * *

GENERIC COMPETITIVE RESPONSE

This section discusses possible competitive responses to the generic segment.

Liggett & Myers

In the absence of any direct competition, L&M will continue to build the generic category. It is almost certain that if Brown & Williamson entered the generic segment, Liggett & Meyers [sic] will react vigorously:

- Generics represent about 60% of L&M's volume. Without generics, L&M's tobacco business would be irreparably damaged.
- Liggett can react. While Liggett may have more short term capacity problems than any other company in the industry if they continue to increase market share, we know that they have ordered seventeen high speed cigarette makers and that would provide them with more than four incremental market share capability. The delivery schedule for this equipment is not known.

We believe the following competitive scenario may be the most likely:

1. L&M first meets Brown & Williamson's offer in the military and categories I and II. In addition, L&M may add full taste, Kings and 100's to their product line and expand sales support. Expansion into full taste could pose a particular threat to KOOL.

   If this happens, we believe Brown & Williamson still has a good chance of securing generic volume due to our ability to

provide better service and the belief that distributors and chains would prefer doing business with us because of our size and perceived stability.

Brown & Williamson would match L&M's move to a full product line. If L&M goes to full sales support, Brown & Williamson would match customer service through one or more of the following: temporarily "borrowing" the B&W sales force and possibly blitzing at wholesale/retail; increasing permanent part-time help; and seeking additional broker resources.

2. If after matching B&W's offer, Liggett begins losing generic volume, or Brown & Williamson is not able to secure new volume, then one of the competitors will spend down to spend full variable margin (i.e. zero profit at $14.08/M for B&W). Assuming that the points are basically similar for both companies (there are insufficient data to conclude otherwise), we would expect the other competitor to match this offer.

3. If L&M goes below our full variable margin, Brown & Williamson would not plan to match their offer.

As such, under all likely scenarios B&W stands to capture a major part of the segment. We would not expect L&M to be able maintain any loss position long term.

It is possible that L&M may choose to retain only the profitable, smaller

accounts, leaving B&W to have the larger, less profitable generic busines [sic] (the opposite scenario is also a possibility).

R.J. Reynolds

We consider Reynolds a likely candidate for entry into generics or a third price point. Further, it is possible that their entry may be accelerated if Brown & Williamson does *not* enter the segment, in order to control it. The reasoning is as follows:

1. If the continued grown of generics is not contained by another company and Reynolds concludes that not only are profits but generics are affecting the company's ability to regain its number one position in the cigarette category, it may be forced to react.

2. Reynolds currently loses more volume to generics than any other company.

R. J. Reynolds Contribution to Generics

Current Smokers	Contribution to Generic Gains	Index
32.6	38.5	(118)

Source: Switching Study, Wave 35

In addition, Winston is currently the largest contributor to generics, providing close to 20% of generic gains (the next highest is Marlboro at about 11%).

Note that from a capacity standpoint, Reynolds sold about 20 billion fewer cigarettes in 1983

than in 1982. It can therefore be assumed that the company has excess capacity at least to this point on a five day work week, and this could increase significantly if a six or seven day work week is considered (as a non-union manufacturer, Reynolds should not have a problem moving to a longer work week).

Reynolds' initial reaction to continued generic growth might be to heavily coupon/discount its branded lines to try and neutralize the generics' advantage. If this tactic is unsuccessful, RJR may launch/reposition a brand at a third price point. A third price point may offer Reynolds more leverage and control than just going to generics, since it can establish its own pricing/margin structure and leverage RJR's sales force strength. In addition, it may be a sounder course of action from a legal standpoint to avoid any possible anti-trust action, which could result from taking on head-to-head a small manufacturer and possibly putting them out of business.

One likely scenario for this price point is that Reynolds would reduce the price on one of its existing marginal brands, such as Doral, which currently has a share of .19 (off 0.05 share points in 1983).

If Reynolds or another competitor entered generics or a third price point prior to B&W, we would of course assess how that scenario affected our proposed program and react accordingly. One likely tactic would be for B&W to move as soon as possible to test a mid-priced brand.

Philip Morris

Similar to R. J. Reynolds, we believe the possibly of Philip Morris' entry is reasonably high, particularly if the segment is not managed by one of the smaller companies. In addition, if Philip Morris' number one position begins to erode, Philip Morris may react regardless if Brown & Williamson enters or not.

1. Philip Morris has a strong rationale for immediate entry. Their brands are image-driven; by entering the generic segment, they put all competitors in a vice between full price/high image offers and generics thereby gaining the potential to dominate both the top and bottom of the category, leaving competition to fight over the shrinking middle.

2. However, there have been rumors of late that Philip Morris may be getting ready to move into the "Value for Money" segment. These unsubstantiated rumors but have come from both the Midwest and New England [sic]. One of these rumors said that Philip Morris or Reynolds would enter the segment if Liggett gets one more share point.

Similar to Reynolds, we deem the possibility of Philip Morris reducing the price on one of its marginal brands as not unlikely. In Philip Morris' case, a possibility might be Saratoga or Philip Morris brand. Saratoga had a .33 share in 1983, -0.01 versus 1982; Philip Morris brand had a .14 share in 1983, also off -0.01 versus year ago [sic].

From a capacity standpoint, Philip Morris sold about the same number of sticks in 1983 than it did in 1982 (204.7 billion sticks versus 204.4 billion sticks). However, Philip Morris has recently modernized their plant in Louisville and is in the process of starting a new factory in North Carolina. It can be assumed that Philip Morris has, or can obtain, the necessary production capacity to react to any demands in the marketplace. Engineering estimates Philip Morris has machines which would provide packing capacity in a three shift, five day work week in excess of 250 billion cigarettes per year, almost 50 billion cigarettes more than they sold in 1983.

American & Lorillard

In the foreseeable future, we believe that the possibility of American or Lorillard entering the Generic segment is relatively unlikely, whether Brown & Williamson competes in this catetory [sic] or not:

1. Neither company has an aggressive tobacco philosophy. In this regard, a statement made about a year ago by an American top executive said that the company's non-tobacco strategy "is aimed at rejuvenating the company, expanding its earning space, reducing its dependence on tobacco and pulling American out of its nostalgia for days when it was the only tobacco company in America". American is estimated to fund the domestic tobacco business only to the extent necessary to provide cost effective manufacturing, advertising and sales promotion and to maintain relatively stable income.

   Similarly, a major objective of Loew's is to maintain a relatively stable cash flow from its tobacco business to fund other businesses.

2. Both companies have been hurt less than fair share by the introduction of generics.

Contribution to Generics by Manufacturer

	Contribution to Current Smokers	Generic Gains	Index
American	7.8	7.5	96
Lorillard	9.6	8.0	83

Source: Switching Study, Wave 35

3. It is unlikely that either American or Lorillard would commit the funds/use of variable margin necessary to compete effectively in the generic category.

From a capacity standpoint, American probably still has significant capacity, based on recent volume/share declines. Lorillard's capacity is not clear. Their volume has held relatively steady since 1979 but Engineering reports they may be operating only on two shifts. In any event, we do not believe Lorillard would commit to large incremental capital expenditures.

LIGGETT & MYERS TOBACCO COMPANY

FEBRUARY 14, 1984

* * * * * AGENDA * * * * *

OPENING REMARKS AND MANAGEMENT PHILOSOPHY	K. V. DEY
MARKETING & SALES STRATEGY	HAL GRANT
OPERATIONS & PRODUCT ASSURANCE	JIM TURNER
FINANCIAL REVIEW	DAVE WELSH
L&M DO BRASIL	DAVE WELSH
ADMINISTRATIVE & LEGAL SUMMARY	K. V. DEY

* * *

GENERIC/PRIVATE LABEL COMPETITION

- DOMESTIC COMPETITION – GET 4 NEW SMOKERS FOR EACH ONE THEY LOSE
  - $3.00 PER M VS. $13.00 PER M MARGIN
  - U.S. DISTRIBUTORS EXTREMELY HAPPY WITH GARY'S STRATEGIC SELLING SYSTEM. "THEIRS NOT OURS".
  - COMPETITION WOULD NOT GAIN INROADS BY MEETING OUR PRICE – WOULD HAVE TO BE SIGNIFICANTLY LOWER.
  - MANUFACTURING WOULD BE LOGISTICAL NIGHTMARE. CURRENTLY NOT SET UP FOR LOW VOLUME PRODUCTION RUNS.

[Handwritten Note]
Final FC 3/9
[March 9, 1984.
See Tr. 30:106]

BROWN & WILLIAMSON GENERIC PROPOSAL

I. *Current Situation*

An economy and value for Money segment are emerging in the U.S. cigarette market. These segments include generic, 25's and mid-priced brands.

Generics have enjoyed phenomenal volume growth since introduction in 1980, growing to over 17.5 billion units in 1983 and achieving virtually full national distribution in all classes of trade lead by supermarkets where generic's distribution has reached 98% nationwide. Projected 1984 volume could exceed 30+ billion units. L&M currently sells 97% of all generic cigarettes.

In addition, R.J. Reynolds created the 25's segment in June, 1983 by launching Century. The brand is currently sold in about 70% of the U.S. and has attained a December, 1983 share of about 1.25% where sold.

Brown & Williamson quickly assessed 25's potential and launched RICHLAND in 20% of the U.S. in September, 1983. RICHLAND had about a .35% share in December, 1983 where sold.

Most recently, in February, 1984, a third price point has been created: Quik Trip Convenience Markets introduced Bronson cigarettes, manufactured by L&M and distributed exclusively by National Products Group. Carton pricing is about 11% more than generics and 13% less than branded 20's. Since this introduction is still in its first month and limited to

one regional chain, it is too soon to assess its viability or potential.

Recent market phenomena – generics' success, 25's introduction, mid-priced offer testing and increasing price discounting – indicate multiple price points will play a significant and increasing role in U.S. cigarette marketing.

To respond to these changing market conditions, Brown & Williamson is developing plans for each component of the emerging economic segment. A go/no go decision for RICHLAND expansion is expected in April, 1984. An analysis and recommendation of B&W's response to the creation of a mid-price point will be compieted by March 26.

This document specifically addresses generics, which represent B&W's most immediate incremental volume opportunity.

II. *Background*

Total industry volume is declining – from 626 billion units in 1981 to 595 billion units in 1983. By 1988, B&W forecasts industry volume will decline to 591 billion units.

Counter to the general market trend, generic sales are growing rapidly. From a launch year volume of only 230 million units in 1980, generics have grown to over 17.5 billion units in 1983, approaching a 3% share of market. Currently generics are selling at an annualized rate of 3.56%. By 1988, using a straight line projection of generics' 1983 growth rate, generics will account for over 14 share points; more than 85 billion annual unit sales.

B&W's contribution to generics is disproportionately high. Specifically, B&W contributes about 70% more

than its fair share volume to generics. B&W losses account for about 21% of generics' gains. In 1983 B&W lost about 3.7 billion sticks to generics, a variable margin loss of over $50MM. By 1988, this loss could total 18 billion sticks and about $350MM lost variable margin.

Unchallenged, L&M could continue its total dominance of this segment and grow to a total company share of over 15% by 1988, becoming the third largest company in the U.S. cigarette market.

Stipulating that the industry's interests – other than L&M's – would be far better served had generics never been introduced, they are an immediate and growing threat to all other manufacturers. Competitive counter-actions are essential and inevitable.

III. *Competitive Response*

Generic growth represents volume erosion for all competitors. Unchallenged, L&M will continue aggressive segment development since it has virtually no stake in the branded, full price market.

All other manufacturers face a shrinking industry and eroding share and volume as generics grow. One or more competitors, particularly Philip Morris, R. J. Reynolds and Brown and Williamson, have the capacity, sales resources and motivation to participate.

1983 Losses to Generics

For perspective, in 1983 cigarette companies lost approximately the following volume and variable margin to generics:

*   *   *

These numbers/trends suggest that competitive response is inevitable and will be significant. Further, *all manufacturers currently have excess capacity available*. By company, we hypothesize the following anticipated competitive actions:

1. *R. J. Reynolds*

   In terms of total volume and variable margin lost to generics, RJR is the most vulnerable company now and in the future.

   Further, RJR has no brand currently able to replace these lost sales; no established RJR brand grew in 1983. Barring a major new brand success (Sterling or other) or an unforeseen turnaround of an existing brand(s), RJR must assault the economy segment to hold share and volume. In response to generics, RJR may pursue one or more of the following strategies:

   Priority One

   Launch a generic product line to gain control of and contain generic segment growth. RJR would strive to limit segment development since incremental generic growth will disproportionately reduce RJR's total margins.

   Priority Two

   Launch a mid-priced brand. This is a RJR's second best option given its:

   a) Sales force size and strength

   b) Domination and control of retail display fixtures

   c) Available list of low volume brands

   These resources position RJR to distribute and sustain a mid-price at retail.

   Priority Three

   Increased discounting of RJR's full line of branded products in an attempt to reduce outflows to generics.

   Priority Four

   Continue and intensify development of the 25's segment through:

   - Century support
   - additional 25's brands
   - shift to 250's cartons

   While RJR may pursue this strategy, the source of business for 25's is currently branded, not generics products. Increased support of 25's does not therefore represent a direct, effective defense against generics' growth.

2. *Philip Morris*

   Given the strength of their branded products, P.M. could choose to stay out of the economy segment and still maintain and increase its hold on industry share leadership.

   However, P.M. may choose to maximize their total volume and share through the following strategies:

Priority One

Launch a generic product line directly competitive to L&M. P.M.'s low vulnerability to generics makes a direct entry attractive as a means to build net incremental volume with disproportionately low cannibalization while inflicting heavy losses on all other competitors, especially RJR and B&W. If P.M. enters generics, they have little reason to restrain segment expansion in the short term.

Priority Two

Launch a mid-priced brand using P.M.'s sales force strength – as can RJR – to establish and maintain a third price point.

Priority Three

Launch a 25's brand. As indicated in the RJR section, 25's are not a direct defense against generics. We, therefore, expect P.M. to track 25's growth and enter the segment when its trend justifies entry on its own merits.

Note: We do not expect P.M. to pursue established brand discounting given their brands' image-driven vitality and P.M.'s stated dismissal of such tactics for other than new products.

3. *American and Lorillard*

For several and different reasons, both companies contribute less than their fair share to generics. Both companies' parents are pursuing cash flow maximization strategies from their tobacco holdings to fund other activities.

However, both companies could, like P.M., choose to enter generics as a source of immediate low risk incremental volume.

Despite their conservative current marketing practices, both Lorillard and American will, along with the rest of the industry, be forced into generics competition in some form if the segment continues on current trend towards 14.5 50M in 1988.

IV. *B&W's Objective and Strategies*

Objectives:

Enter the generic segment to recover lost volume without negative trading profit impact. This objective will be pursued until such time as new branded products are launched and able to replace generic sales with higher margin volume.

1984

Obtain at least 3.7 billion generic unit sales this year.

Strategies

1. Offer an equivalent line of generic cigarettes at a lower net price to displace L&M as the principal generic supplier to select high volume trade customers.

2. Launch total offer in third quarter 1984 to gain volume and establish an immediate trade customer base. If generics grow towards 14.5 50M in 1988, B&W cannot afford to let other major competitors establish segment presence and preempt our future ability to generate volume from generic sales.

V. *Summary Rationale*

Generics represent B&W's most immediate opportunity to increase volume. This volume can be achieved within current manufacturing capacity, without incremental manpower and without negatively impacting trading profit. No other option offers similar potential to recover lost volume/share with such minimal investment risk. This is true because our goal is to capture existing demand . . . not create new consumer demand.

VI. *Generic Business Plan*

Implementation strategies for 1984 have been designed to meet this objective without seriously diverting resources from projects with higher trading profit potential. When higher margin branded products become available, B&W will proportionately reduce its generic sales.

1. *The target customer universe is the top 38 accounts.* While all direct-buying customers are potential candidates for the B&W generic entry, this primary target customer list represents an estimated 8.2 billion generic units per annum (*4.18, last 6 months of 1984*).

   When combined with the *1 billion* units available in Military commissaries (the initial Military target group), this select customer list can provide sufficient volume for successful entry into the generic segment.

   In addition, this strategy will minimize:

   - sales force effort
   - the number of generic labels

2. *The product line will match competitive offerings style-for-style.*

   B&W's generic products will basically match current national brand specifications to enhance production efficiencies. Most, if not all required plant modifications are already covered by the Macon Export Plan.

   To match competition, these styles will be offered:

Ultras	Lights	Plain (Military only)
NM-KS -100	NM-KS -100	70
	M-KS -100	KS

   This strategy calls for minimizing the number of labels required to meet the needs of B&W's priority high volume customers. These minimum requirements include: four black & white generic labels; three reserved for the highest volume customers in each area. Private labels, if any, will be copied as they are the property of targeted customers. The initial Military offering will be one of the above generic labels, but we are prepared to introduce a branded generic (e.g., "Hallmark") if required to gain entry into this important customer segment.

3. *B&W generics will be sold at the same list price, but with superior net costs to the customer.*

   The list price will be \$18.75/M for Kings and \$19.75/M for 100's. No returned goods will be accepted.

   B&W will offer a five level volume discount structure (range: \$.35/carton to \$.15/carton);

the competition's current offer has a more narrow $.15 – .10/carton range.

Various other allowances are offered by the competition and will be met or exceeded on a selective basis. Here is a comparison of the discount/allowance structure:

	Per Carton Discounts			
	L&M		B&W	
	High	Low	High	Low
Total discount allowances:	$.37	$.22	$.47	$.27

Brown & Williamson's offer will produce a full variable margin of $4.64/M and a net variable margin of $4.14/M[1]. B&W is prepared to spend up to net variable margin as a first step response to competitive counter-offers; if required, we are also prepared to go up to, but *not* beyond, full variable margin to gain entry into the generics market.

* * *

Financial Impacts

To attract customers, B&W is prepared to provide total discounts and allowances superior to competition.

These discounts and allowances can absorb all generic variable margin *except* that required to cover incremental overhead and working capital costs.

[1] The $0.50 difference between full and net variable margin represents incremental overhead.

Longer-term, generics may become profitable. At this time, however, B&W is not projecting any profit or return from generics because the magnitude and duration of competitive response cannot be accurately estimated.

From a financial perspective, this proposal can be fully justified on the basis of its optimization of our manufacturing capabilities, its ability to carry its appropriate share of overhead, its assurance that financial losses on generics will not occur, and its ability (particularly if B&W's presence displaces L&M and/or preempts other competitors) to slow our branded, high margin losses to generics.

VIII. *Liggett and Meyers* [sic] *Response*

In the absence of direct competition, Liggett and Meyers [sic] will continue to develop the generic category. When any cigarette competitor enters the generic category, L&M will almost certainly react vigorously.

To survive a competitive entry, L&M can be expected to minimally match the competitive offer, at least in the Military and their largest volume accounts. Further, L&M may spend down to full variable margin (i.e., zero profit). Conservatively accepting that generics will attain about 24MM units in 1984, of which L&M might secure 20MM, it would cost L&M an additional $35-45MM in lost variable margin to defend its business (assuming a competitor entered in June and Liggett defended in the 3rd and 4th quarters first by matching and then by going to a zero profit position).

It is also likely that L&M will consider a number of tactical moves, including:

- improving customer service by providing direct sales support

- adding code dating to improve product quality/aging tracking on the shelf
- line extending into full taste (including a KOOL-type menthol)

Brown & Williamson would be prepared to match any improvement in service level or line extension. If L&M goes below full variable margin, Brown & Williamson would not plan to match their offer. We would not expect L&M to be able to maintain a loss position for any extended period of time.

Note that any moves by L&M to augment sales support in the Military would necessarily drain resources from its civilian operations.

IX. *Industry Response to B&W Generic Entry*

If B&W launches a generic entry, we believe the most likely competitive response is a company-by-company re-evaluation of their respective plans for the economy and Value-for-Money segments. In the case of R. J. Reynolds and Philip Morris, the most likely candidates for entry, B&W's entry would force re-evaluation and reprioritization of their options (e.g., generic versus 25's versus mid-price point) and their timing of any planned introduction. Specifically, B&W's generic strategy will reduce any anticipated profit potential generics now offer. To gain a competitive advantage, competition must reduce margins further or divert key resources such as sales force time from higher margin established brands.

X. *B&W Response to an R.J. Reynolds or Philip Morris Generic Introduction*

A generic entry for Brown & Williamson whose purpose is to recover lost volume until such time as full margin new products can be launched makes

sense irrespective of whether R. J. Reynolds, Philip Morris (or both) introduce a generic either in response to B&W or before B&W. Specifically:

R. J. Reynolds or Philip Morris follow B&W into Generics

In this case, B&W is in a good position to retain much of the generic volume it has gained. This is because we are prepared, through various discounts, to spend down to full variable margin (zero profit) and RJR/PM should not be able to make their offer meaningfully more attractive since they are probably unwilling to risk selling below cost which in many situations would be evidence of unlawful conduct. (Law [. . .]

REDACTED

RJR or PM may have some flexibility to offer deeper discounts than B&W due to cost efficiencies in their operation which, if they exist at all, probably would trace to the use of offshore leaf. However, we judge that any such cost differential would be relatively minor and would translate to small enough variation in our and competitive discount structure so as to make the trade disinterested in going through the burden of changing generic suppliers.

Note that if RJR or PM take other steps, such as improving generic customer service, line extending, offering a returned goods policy, etc., we would be prepared to competitively match any such tactical move.

RJR or PM introduce generics before B&W

Under this scenario, B&W would move to enter the generic segment as soon as possible and be prepared to spend up to full

variable margin, targeting to gain as much large customer business as possible.

XI. *Next Steps*

This recommendation requests approval to initiate key trade customer contacts as the first step towards a third quarter launch. These contacts are essential to confirm our generic segment analysis and to assess our program's *incremental* sales generation potential.

If we find in this process unanticipated problems or if market conditions shift significantly, B&W will reconsider and modify this proposal as required. With these caveats, B&W can be prepared to enter the generic segment in the third quarter, 1984.

REDACTED

[Handwritten note]

file
current 1092 [illegible]

MEMORANDUM

TO: I. W. HUGHES
J. ALAR
W. L. DeWITT
T. E. SANDEFUR

FROM: J. A. McDONOUGH

SUBJECT: *1984 STRATEGIC PLAN AND 10 YEAR FORECAST*

DATE: MARCH 9, 1984

Attached is your copy of the 1984 Strategic Plan and 10 Year Forecast and cover letter to Mr. McCarty.

/s/ J. A. McDonough
J. A. McDonough

attachment

/mjs/1833J

* * *

B&W

BROWN & WILLIAMSON TOBACCO CORPORATION

1984 STRATEGIC PLAN

AND 10 YEAR FORECAST

RESTRICTED **FEBRUARY 1984**

* * *

For American, a generic launch represents a relatively low cost, low risk source of incremental volume.

Although its parent company has been pursuing a strategy to maximize cash flow, American could be forced or decide to enter the economy segment. However, over the longer term, increased tobacco industry competition and higher resulting support levels could cause American to pursue a more aggressive cash maximization/sale approach.

Loews

Loews appears required to continue to use its tobacco business to somewhat insulate its corporate portfolio from earnings declines in other lines of businesses. Continued financial restructuring of Loews and potential sales of some non-tobacco property and businesses would be expected in 1984. Potential lower future industry profit margins and an improved U.S. economy, could imply that Lorillard could adopt a harvesting strategy.

However, for Lorillard, generics would represent a potential source of additional volume which would afford minimal risk to their established brands and require limited resources. They, like American, could be forced or decide to enter the generic market in some form if the segment continues its current trend.

Liggett & Myers

L&M's dramatic success with generics, combined with significant cost reductions over the past several years, has bolstered L&M's confidence to expand new branded product activities, although within a narrowly segmented approach. It would be estimated that L&M's future success and volume of activity in branded products will be

established using specific financial criteria. L&M can possibly husband its allocated funds by the elimination or recombination of duplicate Gary Tobacco activities as generics are a firmly established cigarette segment. Most recent announcements of a potential leveraged buyout of L&M would imply that L&M's new owners would be significantly more dependent upon generic/private label cigarettes for the company's viability.

In the absence of direct competition, Liggett & Myers will continue to develop the generic category. When any cigarette competitor enters the generic category, L&M will almost certainly react immediately and vigorously. However, it is unlikely L&M can, in fact, be prepared to engage in a sustained battle because it does not have the financial resources of others in the industry.

BROWN & WILLIAMSON TOBACCO CORPORATION

INTERNAL CORRESPONDENCE

TO	Dr. I. W. Hughes
DEPT.	Mr. T. E. Sandefur, Jr.
	Mr. J. Alar
C.C. to	Mr. J. McDonough
"	Mr. C. Heger
"	Mr. D. Falk
FROM	Mr. R. A. Blott
DATE	March 22, 1984
SUBJECT	Eric Bruell's Telex Dated March 21, 1984

This will address the questions raised by Eric Bruell with regard to our generic proposal. Before getting into specifics, however, it should be noted that Eric's overall conclusion was contingent upon gaining more knowledge on the LIFO effects of the recommendation. Carl Heger has concluded that the sale of 6 billion units of generics in 1985 and beyond would eliminate all LIFO decrements between 1984 and 1988. This would represent $19 million if we included forecasted new products and $81 million if excluded new products (see attached memo).

Now for the specific questions.

1. *Projected Growth Rate of Generics*

   We do not believe this is a substantive issue. The fact is that we have already lost significantly on a volume and margin basis; we continue to lose disproportionately and that we can expect these losses

   to continue if generics achieve *any* kind of future growth. We can abate these losses – certainly in a volume and share sense, and, to a limited degree in a financial sense, by an absorbtion of overhead and a modest return in generics simply by participating in the volume generics have already achieved.

   Setting these views aside, we are preparing estimates of impacts assuming generics only grow to 7% of total market by 1988 (vs. 14%) and B&W's losses are 1.3 x fair share and 2.0 x fair share (vs. 1.7x).

2. *B&W's Entry Will Increase Total Generics And Might Provoke Competitor Reactions.*

   The future growth of generics will be driven by consumer demand – not by the number of manufacturers who supply those products. The level of consumer demand will be a function of the price/value relationship, the image reinforcement needs of smokers and the level of retail distribution.

   The B&W proposal is based on offering greater discounts – not reducing the list price. Since retail pricing is based on list prices, B&W's generics will not enhance the price/value relationship of present generics.

   On the image front, there are obviously a certain number of smokers who are prepared to make the trade-off and they will do so irrespective of B&W.

   On the distribution side, generics are already available in 98% of all commodity grocery volume and in approximately 65%-70% of all commodity cigarette volume. Future distribution gains will be limited and slow in coming. Further, B&W proposes selling against accounts already selling generics, thus displacing L&M.

As for provoking a competitive response from L&M or others, we suggested this was quite likely in our proposal. The decline in consumption and the growth in generics has removed 60 billion cigarettes from branded manufacturers in just three years. A competitive response appears to be inevitable and we strongly feel B&W will be better off being second rather than third or fourth.

3. *B&W's Credibility Will Suffer. This Initiative Will Conflict With Intention To Create Image As Leader In Innovation.*

Credibility is based upon the development of a successful business. One could argue that B&W's entry into generics could be viewed very positively –both in the sense of being aggressive in recapturing volume and in the sense of identifying an emerging segment and moving forcefully to establish a position in the new segment.

Innovation can come on many fronts – product, packaging, pricing, marketing, etc. Entry into generics with a strong program seems to be more innovative than letting a new segment emerge and get away from us.

4. *Financial Implications Of Generic Entry Need To Be Spelled Out And Compared To No Action. 25's/250's And Establishing A New Price Point.*

As noted previously, determining the financial implications of various scenarios is underway. Under any set of assumptions, the question of losing by not participating is not the issue – rather, it is determining the amount of the loss.

[Illegible] [March 22, 1984. *See* Tr. 47:33]

This will address questions raised by Eric Bruell with regard to our generic proposal. Before getting into specifics, however, it should be noted that Eric's overall conclusion was contingent upon gaining more knowledge on the LIFO effects of the recommendation. The Five Year Plan projects LIFO decrements of $11.2 million in 1984 and $7.8 million in 1985. Finance has advised that the sale of 4 billion units in 1985 would eliminate the decrements entirely.

Now for the specific questions.

1. *Projected Growth Rate of Generics*

We do not believe this is substantive issue. The fact is that we have already lost significantly on a volume and margin basis; we continue to lose disproportionately and we can expect these losses to continue if generics achieve *any* kind of future growth. We can abate these losses – certainly in a volume and share sense, and, to a limited degree in a financial sense, by an absorption of overhead and a modest return in generics simply by participating in the volume generics have already achieved.

To demonstrate this impact, Finance has computed Trading Profit under four scenarios. Two scenarios assume generics stay at 5% share (January, 1984 level) and B&W's diversion declines to 1.3x its fair share or grows to 2.0x its fair share (current is 1.7x). The last two scenarios assume generics grow to only 8% of the market with the same diversion ratios (1.3x, 2.0x).

The following tables summarize the results.

Generic Impact on B&W Trading Profit
Assuming B&W Does Not Enter

	1984	1985	1986	1987	1988
Generics @ 5.0%					
1.3x Annual	(49.3)	(52.0)	(54.3)	(57.7)	(59.4)
Cume	(49.3)	(101.3)	(155.6)	(213.3)	(272.7)
2.0x Annual	(75.6)	(81.1)	(84.7)	(88.0)	(90.6)
Cume	(75.6)	(156.7)	(241.4)	(329.4)	(420.0)
Generics @ 8.0%					
1.3x Annual	(49.3)	(67.7)	(87.4)	(92.3)	(95.3)
Cume	(49.3)	(117.0)	(204.4)	(296.7)	(392.0)
2.0x Annual	(75.6)	(105.3)	(135.0)	(141.3)	(146.9)
Cume	(75.6)	(180.9)	(315.9)	(457.2)	(604.1)

This clearly demonstrates the impact of generics upon B&W. If generics just maintained current share (5.0%) and B&W's diversion declined to 1.3x fair share (which is highly unlikely), the loss in trading profit is $272.7 million over the next five years. Any increase in generic share or diversion severely increases the impact on B&W.

2. *B&W's Entry Will Increase Total Generics and Might Provoke Competitor Reactions.*

The future growth of generics will be driven by consumer demand – not by the number of manufacturers who supply those products. The level of consumer demand will be a function of the price/value relationship, the image reinforcement needs of smokers and the level of retail distribution.

The B&W proposal is based on offering greater discounts – not reducing the list price. Since retail pricing is based on list prices, B&W's

generics will not enhance the price/value relationship of present generics.

On the image front, there are obviously a certain number of smokers who are prepared to make the trade-off and they will do so irrespective of B&W.

On the distribution side, generics are already available in 98% of all commodity grocery volume and in approximately 65%-70% of all commodity cigarette volume. Future distribution gains will be limited and slow in coming. Further, B&W proposed selling against accounts already selling generics, thus displacing L&M.

It is doubtful that B&W would lose more of its smokers to a B&W generic since manufacturers of generics would be loath to identify their company on the generic packs. As noted above, B&W would displace the current generics at retail – not sell along side current generics.

As for provoking a competitive response from L&M or others, we suggested this was quite likely in our proposal. The decline in consumption and the growth in generics has removed 60 billion cigarettes from branded manufacturers in just three years. A competitive response appears to be inevitable and we strongly feel B&W will be better off being second rather than third or fourth.

L&M will attempt to retain this business but lacks financial strength to cover all fronts on a sustained basis.

3. *B&W's Credibility Will Suffer. This Initiative Will Conflict With Intention To Create Image As Leader In Innovation.*

Credibility is based upon the development of a successful business. One could argue that

B&W's entry into generics could be viewed very positively – both in the sense of being aggressive in recapturing volume and in the sense of identifying an emerging segment and moving forcefully to establish a position in the new segment.

Innovation can come on many fronts – product, packaging, pricing, marketing, etc. Entry into generics with a strong program seems to be more innovative than letting a new segment emerge and get away from us.

4. *Financial Implications Of Generic Entry Need To Be Spelled Out And Compared To No Action, 25's/250's And Establishing A New Price Point.*

The financial implications of not participating in generics were described earlier. Finance has run two scenarios with B&W participating. The first assumes generics grow to 5% and B&W enters in 1984 and captures 50% of this segment by 1986. The second assumes generics grow to 8% with the same entry and capture ratio by B&W.

Trading Profit Impact
B&W Enters Generic Market

	1984	1985	1986	1987	1988
Generic 5.0%					
Annual	(9.3)	(27.0)	(57.0)	(69.0)	(81.2)
Cume	(9.3)	(36.3)	(93.3)	(162.3)	(243.5)
Generic @ 8%					
Annual	(9.3)	(44.7)	(91.1)	(110.5)	(129.6)
Cume	(9.3)	(54.0)	(145.1)	(255.6)	(385.2)

Brown & Williamson Tobacco Corporation
INTERNAL CORRESPONDENCE

TO:	E. T. Parrack		
CC:	T. E. Sandefur R. A. Blott	D. P. Christensen D. J. Bores	
FROM:	D. I. Falk	DATE:	April 26, 1984

SUBJECT: *Generic "Black and White" and Private Label Offerings Versus Branded Generic Offering*

This provides the pros and cons for two potential Brown & Williamson price offerings:

- *Generic "Black and White" and Private Label Offerings*
  - Brown & Williamson would offer an equivalent line of generic cigarettes to L&M at the same list price but at a lower net price (via greater merchandising and volume discounts).
- *Branded Generic Product (code name Hallmark)*
  - Brown & Williamson would offer a branded generic line-up (e.g., full taste and lights Ks and 100's, menthol and non-menthol) at the same list price as L&M. Instead of merchandising and volume discounts, the brand would be supported with B&W advertising and promotion.

Summary – The following page summarizes the pros and cons of these two propositions. This is then followed by a more detailed discussion.

Generic Comparison

"Black & White" and Private Label

Pros

1. Greatest immediate volume opportunity
2. Better limit generic segment cannibalization of B&W branded volume
3. Requires no investment spending
4. Superior short-term financial proposition
5. Merchandising/returned goods responsibility shifted to the Trade
6. Greater manufacturing overhead absorption/flexibility

Cons

1. May produce major competitive response (particularly L&M)
2. More difficult from a manufacturing standpoint (number of iterations)
3. Possibly greater legal risks
4. Not certain that can displace L&M
5. No initial load-in

Branded Generics

Pros

1. From a volume standpoint, more latitude to go after full taste segment
2. Has dual appeal of low price plus imagery
3. May provide a quality reassurance
4. Consumers can find the same brand in all outlets (not possible with "Black and White" generics where there are four variations)
5. Has greater advertising and promotion opportunities
6. Easier to manufacture (because less variations)
7. May be more defendable competitively
8. Initial pipeline volume

Cons

1. No guarantee of retail price level
2. Will require considerable investment spending
3. Could accelerate price segment growth and therefore cannibalization
4. Proposition of branded quality at generic pricing may not be believable
5. More difficult to secure merchandising
6. Return goods B&W responsibility
7. May be difficult to sell to chains which have own private label

Details

I. *Generic "Black and White" and Private Label*

A. *Pros*

1. *This appears to represent the greatest immediate volume opportunity for Brown & Williamson in the price segment.*

   - This segment has already proven its viability, with 1983 sales of over 17.5 billion sticks (3.0 share points). Alternatively, branded generics are at this time a basically untested idea.

2. *This proposition provides Brown & Williamson with the best opportunity to contain cannibalization of its full revenue branded products.*

   - B&W sales would replace current L&M generic volume and not be incremental, based on the assumption that the retailer need carry only one generic line since there would be little or no differentiation among different lines. Therefore, while cannibalization would still exist, it would be less than with a branded generic which would tend to increase the price segment.
   - Managing cannibalization is key since B&W has been losing disproportionately to generics (170 index versus fair share loss).

3. *This proposition requires no investment spending to be successful.*

   - Because we would be seeking to displace Liggett as opposed to building totally

new incremental volume within the industry, there would be no need to promote or advertise heavily to the consumer.

4. *This represents a more attractive financial proposition to the Company, at least in the short term.*
   - Since "Black and White" plus private label generics do not require investment spending, the proposition pays out immediately and continues to pay out as you go.

5. *Due to the fact that "Black and White" and private label generics are basically the retail trade's product, they have the added benefit of transferring merchandising and returned goods responsibility to our customers.*
   - B&W Sales Force involvement will be limited.
   - There may be the added benefit of improved trade relations (and benefits to our branded line) to the extent that customers conclude that we are providing them a service (by producing *their* generic product).

6. *This proposition allows B&W the most flexibility in managing its manufacturing capacity because we can target customers initially since they are under contractual arrangements.*
   - A branded generic offers less initial manufacturing flexibility because it will be

non-contractual and therefore not targetted [sic], and will be treated by the trade as a normal list item.
   - This flexibility is also key assuming B&W wants to diminish its generic business at some future date (as more full revenue brands are available). It would be easier to manage down generic volume with accounts selling "Black and White" product under contract, than it would be to dial down branded generic volume sold in non-contractual outlets.

B. *Cons*

1. *This proposition may elicit a stronger competitive response than branded generics.*
   - From the perspective of L&M, we would be competing directly with the major part of their total business. If a price war erupted – and if lower prices were passed on to the consumer, widening the price gap between generics and premium cigarettes – there is the possibility of increasing cannibalization.

4/30/84

Attached is the telex which is being forwarded to London.

I. W. H.

* * *

R.J.R. DORAL INTRODUCTION

Previous reports forwarded were the news wire release dated 4/27/84 and the investment community report entitled *Doral Backgrounder.*

This report covers verbal feedback from various trade factors based on their calls to R.J.R. To the best of our knowledge, presentation to the trade begins tomorrow (5/1/84).

1. The list price for KS will be $18.75. This is comparable to Liggett's generic pricing.
2. There will be some form of volume rebates, but the exact amounts have yet to be determined. It would appear that the volume rebates will be proportional or somewhat greater than Liggett.
3. The terms are 3.25%, 30 days. This is standard introductory terms and whether or not the 30 days will remain permanent is yet to be seen.
4. 12 states have been identified so far and are as follows: Ohio, Kentucky, Indiana, West Virginia, Kansas, Arkansas, Pennsylvania, North Carolina, South Carolina, Tennessee, Virginia and Mississippi. One of our customers was advised that these twelve states will represent 40% of the generic volume.

Additional information will be forwarded as quickly as it becomes available.

4/30/84
RAB/eah

DATE: May 1, 1984

SUBJECT: *Generic "Black and White" and Private Label Offerings Versus Branded Generic Offering*

This provides the pros and cons for two potential Brown & Williamson price offerings:

- *Generic "Black and White" and Private Label Offerings*
  - Brown & Williamson would offer an equivalent line of generic cigarettes to L&M at the same list price but at a lower net price (via greater merchandising and volume discounts).
- *Branded Generic Product (code name Hallmark)*
  - Brown & Williamson would offer a branded generic line-up (e.g., full taste and lights Ks and 100's, menthol and non-menthol) at the same list price as L&M. Instead of merchandising and volume discounts, the brand would be supported with B&W advertising and promotion.

Summary – The following page summarizes the pros and cons of these two propositions. This is then followed by a more detailed discussion.

Generic Comparison

"Black & White" and Private Label

Pros

1. Greatest immediate volume opportunity
2. Best opportunity to limit generic segment growth and cannibalization of B&W branded volume
3. Requires no investment spending
4. Superior short-term financial proposition
5. Merchandising/returned goods responsibility shifted to the Trade
6. Greater manufacturing overhead absorption/flexibility

Cons

1. Potential competitive response
2. Manufacturing complexity (many styles)
3. Legal risks
4. Not certain that can displace L&M

Branded Generics

Pros

1. Has dual appeal of low price plus imagery
2. May provide a quality reassurance
3. Consumers can find the same brand in all outlets (not possible with "Black and White" generics where there are four variations)
4. Manufacturing simplicity (four styles)
5. May be more defendable competitively

Cons

1. No guarantee of retail price level
2. Requires heavy investment spending
3. Low potential to return growth of generic segment
4. Proposition of branded quality at generic pricing may not be believable
5. Difficult to secure distribution and merchandising expensive
6. Return goods B&W responsibility
7. May be difficult to sell to chains which have own private label

Details

I. *Generic "Black and White" and Private Label*

A. *Pros*

1. *This appears to represent the greatest immediate volume opportunity for Brown & Williamson in the price segment.*

   - This segment has already proven its viability, with 1983 sales of over 17.5 billion sticks (3.0 share points). Alternatively, branded generics are an untested idea.

2. *This proposition provides Brown & Williamson with the best opportunity to contain cannibalization of its full revenue branded products and limit segment growth.*

   - B&W sales would replace current L&M generic volume and not be incremental, based on the assumption that the retailer need carry only one generic line since there would be little or no differentiation among different lines. Therefore, while cannibalization would still exist, it would be less than with a branded generic which would tend to expand the economy segment.

   - Managing cannibalization is key since B&W has been losing disproportionately to generics (170 index versus fair share loss).

   - Direct competition with L&M will force them to defend their current business,

reducing funds available to support further business-building.

3. *This proposition requires no investment spending to be successful.*

   - Because we would be seeking to displace Liggett as the source to existing generic business, there would be no need to promote or advertise heavily to the consumer.

4. *This represents a more attractive financial proposition to the Company, at least in the short term.*

   - Since "Black and White" plus private label generics do not require investment spending, the proposition pays out immediately and continues to pay out as you go.

MEMORANDUM

May 2, 1984

TO: D. I. Falk

FROM: Jim Hite

SUBJECT: COMPETITIVE ACTIVITY - DORAL

The following information has been obtained from the Bosart Co., Springfield, OH concerning Doral:

Product:	Doral Regular Kings and 100's Doral Menthol Kings and 100's
Manufactured by:	R. J. Reynolds
Date of Introduction:	May 11, 1984
Area of Introduction:	13 states (OH, KY, IN, WV, KS, AR, PA, NC, SC, TN, VA, MS, MO)
Price:	\$18.75 per M Kings \$19.75 per M 100's
Introductory Period:	May 11 - June 8
Introductory Discount Allowance:	\$9.60 per *allocated* 12M case. Allowance will be deducted from invoice.
Terms:	3 1/4% - 30 days

NEW DORAL CHALLENGES
LOW-PRICED BRANDS

[Handwritten Note]
Rec'd from Bert Trompter

DIRECT ACCOUNT FACT SHEET
DORAL FILTER AND MENTHOL KING/100'S

Product

New DORAL Filter and Menthol King 100's is the first established cigarette to be introduced as a low-priced brand. In contemporary packaging, DORAL will feature a rich blend and a standard filter, offering smokers a high quality brand name cigarette at a new low price.

Advertising

During the introductory period, an impactful newspaper advertising campaign will support the introduction of DORAL Filter and Menthol King 100's

Promotional Support

- DORAL will be featured prominently in supplemental package and carton displays.
- During DORAL's introduction, in-store merchandising will generate consumer awareness and trial

Introductory Discount Allowance

- $9.60 payment per *allocated* 12M case of DORAL Filter and Menthol King 100's *purchased* during the introductory period.
- Terms: 30 days, 2% cash discount, 1¼% anticipated allowance.
- Allowance will be deducted from invoice

Distribution Incentive Program

- Per case payment on all DORAL cases purchased and delivered during a calendar quarter

Cases per Quarter	Allowances per Case
0-99	$1.80
100-199	$3.00
200-299	$6.00
300-399	$7.20
400-499	$8.40
500 Plus	$9.60

- Incentive Case Allowance will be paid by check or credit memorandum on a quarterly basis

Production Information

	Case Size	Weight	Cube	UPC		
				12M Case	Carton	Pack
DORAL F. 85's	12M	30.0 lbs.	2.4	12300-15112	12300-15113	12300-00051
DORAL M. 85's	12M	30.5 lbs.	2.4	12300-15712	12300-15713	12300-00057
DORAL F. 100's	12M	35.1 lbs.	2.8	12300-15212	12300-15213	12300-00052
DORAL M. 100's	12M	35.6 lbs.	2.8	12300-15812	12300-15813	12300-00058

[In Evidence 5/4/84]

[Handwritten Notes]
[Illegible]

B&W STRATEGIES FOR ECONOMY CIGARETTES

[Handwritten Notes]

Black & Whites

[Illegible]

I. *Summary*

The economy segment continues to grow and expand. Generic sales now exceed four percent of industry, making them the seventh largest "brand." Based upon our present knowledge of the RJR launch of Doral at generic prices[1], it is now totally predictable that this segment will expand and grow. History, to date, indicates that the Doral action will enhance cannibalization of branded items, although it is clear that it is RJR's intention to narrow this effect to black and white or private label brands.

[1] Fourteen states and the military, representing 39% of total cigarette sales.

Given B&W's extreme vulnerability in this segment (170 index contribution versus S.O.M.), the company can expect further and increasing losses to economy propositions.

To counter this growing threat and to exploit the volume opportunities both unbranded and branded generics represent, B&W recommends immediate execution of two strategies:

A. The first strategy is to displace L&M as the supplier of black and white/private label generics. This will be achieved by national introduction of generic (black and white and private label) styles comparable to Liggett's with superior selling allowances, therefore a lower net (not list) selling price. Plan of action to be followed is exactly as our previous proposal outlined.

B. Launch Hallmark as a branded generic, following precisely the pathway of RJR. Consideration has been given to other brand names, including established brands. Established brands were

rejected due to financial penalties. The only other immediate option is Falcon and we do not own that mark in the USA.

This two-prong approach is required since neither strategy alone can effectively exploit the volume opportunities that branded and unbranded generics represent. This approach exploits all visible avenues for the foreseeable future.

II. *Background*

A. Through March, 1984, generic share continues to grow and now exceeds 4.0% of the market.

B. B&W's vulnerability to generics is the greatest of all companies: a 170 index to share.

C. L&M's March, 1984 price increase ($1.50/M) improves generic profitability making the segment more financially attractive to other manufacturers. This raises the probability of competitive entry. The key future player in black and whites is RJR-lack of success with Doral will undoubtedly lead to their launching a black and white.

D. B&W has the capacity to supply new generic, private label and branded generic offers without any adverse affects on the key new product elements of the 5-year plan.

E. RJR's announcement of Doral's repositioning adds volume potential to the economy segment by offering branded quality reassurance to low price positioning. Further, RJR's aggressive fixture merchandising program is designed to provide retail presence for Doral and will attempt to limit generic in-store presence. Doral will offer four low-tar styles: KS/100's in regular and menthol.

III. *Implications*

The Doral repositioning further expands the economy segment: a branded offer can attract price-conscious smokers who have rejected unbranded/private label generics if the retail price point can be maintained. The impact of [illegible] West price reduction in Germany indicates how much incremental share can be moved to low-priced brands by the addition of a branded line to unbranded generics if the price can be maintained. The German experience, plus our own work, show that low price branded offers do not replace unbranded volume: they draw new smokers to the economy segment.

To compete effectively, B&W must offer both unbranded and branded styles.

RJR's Doral repositioning will draw consumer attention to branded generics and create distribution for them. B&W can exploit this opportunity with Hallmark with minimal investment and taking advantage of RJR's consumer communication of the branded generic concept.

Immediate execution of both strategies provides the snyergy required if B&W is to gain a meaningful level of participation in the economy segment, avoid further competitive preemption, and realize volume potential. In the area of competitive response, PM is rumored to be evaluating four fully-branded economy offers (three new trademarks and one existing brand).

The dual approach of the Hallmark and black and whites will give B&W the opportunity to gain greater participation in the economy segment. Longer term, this participation should provide B&W more influence to manage up the prices of branded generics to improve profitability.

It is also clear that all manufacturers must aggressively manage full revenue brand pricing to mitigate the profit impact of branded and unbranded generic growth.

In combination, these factors represent a major restructuring of the U.S. cigarette market dynamics.

IV. *B&W Program Summary*

A. Launch a full line of black and white and private label styles:

1. Same style array as L&M
2. Same list price
3. Superior discounts/allowances

B&W will be prepared to spend full margin in order to displace Liggett & Myers as the trade source of generic and private labels.

B. Launch four styles of Hallmark at generic price:

1. Same markets as Doral
2. Lights: regular, menthol, king, 100's
3. Same terms/allowances as Doral
4. Invest a portion of available margin to buy shelf space on RJR's Doral fixtures or existing generic fixtures and in-store merchandising support. No consumer-marketing effort planned.

V. *Financial Implications*

A. *Black and White/Private Label*

The B&W plan of being a supplier of black and white/private label generics is exactly the same as our previous generic proposal. Assuming 1984

and 1985 sales quantities of 2.2 billion and 15.2 billion, respectively, Trading Profit would be $5.1 million for 1984 and $43.6 million for 1985. However, in order to ensure customer participation and/or defend competitive counterattacks, B&W is prepared to redistribute this entire amount in the form of additional trade allowances. Exhibit I attached provides a summary of the financial implications and major assumptions.

B. *Hallmark – Branded Generics*

B&W's second strategy introducing Hallmark as a branded generic in four styles assumes a start ship date of August, 1984. Assuming sales of .7 billion in 1984 and 2.1 billion in 1985, there would be a break even position achieved at Trading Profit in 1984 and an estimated $4.1 million Trading Profit in 1985. Exhibit II attached provides a summary of the financial implications and major assumptions.

C. *Impact of Doral on B&W*

As noted previously, the Doral action will enhance cannibalization of branded products, and B&W can expect to contribute more than its current share of market. Assuming Doral eventually attains a 1.5% share of market and B&W contributes two times its share of market (22%), then B&W's lost sales quantities for 1984 and 1985 would approximate 300 million and 700 million respectively. The estimated reduction in Trading Profit would be $3.7 million in 1984 and $8.8 million in 1985.

BLACK AND WHITE/PRIVATE LABEL FINANCIAL ASSUMPTIONS

The current Generic proposition will be alike in every way to the original February proposition, with the exception the first ship date would be August, 1984 rather than June 1, 1984.

Projected Sales Volumes are as follows:

1984		1985			
Aug.	.12	Jan.	.74	July	1.40
Sep.	.25	Feb.	.80	Aug.	1.49
Oct.	.49	Mar.	.95	Sep.	1.53
Nov.	.62	Apr.	1.10	Oct.	1.55
Dec.	.68	May	1.20	Nov.	1.58
		Jun.	1.30	Dec.	1.60
Total	2.16B				15.24B
Use	2.2B				15.2B

Selling Prices assumed to be as follows:

1984 – assume no additional increases in 1984 from current 5/3/84 prices

Type	%	Price	Less Discount 2%	Net Price
Kings	51	18.75	.375	18.375
Longs	49	19.75	.395	19.355
Average	100	19.24	.385	18.855

1985 and Forward

Basis will be to assume the same relationship of Generic to Premium priced products that would exist in 1984:

	Kings			Longs		
	Full	Generic	%	Full	Generic	%
5/3/84 Gross	$29.15	$18.75		$30.15	$19.75	
Discount	3¼%	2%		3¼%	2%	
Net Price	$28.203	$18.375	65.2	$29.170	$19.355	66.4

Assume 65%

[Handwritten Note]

Generics 5/15/84 London

Background

Prior to 1982, the Domestic U.S. cigarette market realized a compounded unit growth rate of 1.3% over a 10 year period. Total industry shipments increased from 549.9B in 1972 to 626.1B in 1981. Manufacturer's price increases generally were below the rate of inflation but margins improved handsomely due to favorable leaf prices and cost reductions associated with automation. For example, Brown & Williamson's variable margin increased from \$2.91/M in 1972 to \$8.78/M in 1981, an increase of over 200%. In 1982, the industry became much more aggressive on the pricing front, fueled by a 100% increase in the Federal Excise Tax. Brown & Williamson's variable margin increased from \$10.78/M in 1982 and to \$12.61/M in 1983.

The impact of these pricing activities on the smoking public was dramatic. The weighted average retail price of a pack of cigarettes increased 56% between 1980 and 1983 (from \$.63 to \$.98). These increases, in combination with the continued health controversy and a recession, led to a decline in industry shipments in 1982 to 622.3B (-.6%). Shipments declined more severely in 1983 to 595.9B (-4.2% versus 1982). Between 1981 and 1983 total industry shipments declined 30.2 billion units.

Emergence of Economy Priced Segment

Coincident with the above, the smallest of the Domestic U.S. manufacturers was on the verge of going out of

business. Liggett & Myers' share had declined to 2.33% in 1980 and none of its brands were progressive. However, seeing the margins which were available, L&M made the bold move of introducing a generic black and white package at a substantial price discount. While selling only 230 million units in 1980, L&M has expanded the business to over 4 share points in the first quarter of 1984.

L&M has built the generic business with a well thought-out and elaborate plan involving both distributors (black and white labels) and direct retail accounts (private labels). It is presently estimated that 80% of this business is in black and white offerings and 20% is in private labels.

This is the first time that a manufacturer has used pricing as a strategic marketing weapon in the U.S. since the depression era. At that time, when economic conditions were more severe than at present, low price brands captured approximately 23% of the market before the dominant manufacturers dropped their prices on full priced brands, thereby limiting the low price entries to 10%-14% market share during the 1930's.

Current Situation

L&M's successful development of the generics/private label segment has come from all manufacturers. However, Brown & Williamson has lost disproportionately and R. J. Reynolds has lost the most absolute volume as summarized below.

1983 Losses to Generics

	Contribution To Generics*	Fair Share Loss	Volume Loss (BB Sticks)	Variable Margin Loss** ($MM)
	%	Index		
American	7.0	(83)	1.28	16.3
Brown & Williamson	21.1	(170)	3.78	48.2
Liggett & Myers	3.0	(120)***	.58	7.4
Lorillard	8.0	(83)	1.48	18.9
Philip Morris	22.7	(73)	3.98	50.7
R.J. Reynolds	38.2	(118)	6.78	86.4
Total			17.88	227.9

*Based on Switching Study, Waves 34 & 35
** Assumes $12.75/M Variable Margin
*** Excluding generics

Brown & Williamson's disproportionate loss is a function of the nature of its brand franchises. Brown & Williamson's smokers are generally older and more down-scale than the balance of the industry.

Given RJR's recent loss of industry leadership, its large and continuing losses to generics and its stated objective of regaining leadership through a product line strategy of having entries in all viable segments, it is not surprising that RJR has just launched the first branded generic. RJR is repositioning an established brand (Doral .2% SOM) and has introduced it nationally in the military and in 14 states in the civilian market. The list price of Doral in the civilian market is comparable to Liggett & Myers' generic and RJR has announced an aggressive merchandising program, superior discount structure and a newspaper advertising program. In the military, RJR has launched at a *lower* list price than generics ($16.95/M versus $18.25/M).

Strategic Conclusions

The RJR stated position in its announcement of its plans to introduce Doral at generic prices was to participate in the emerging economy price segment. A VICEROY pricing test was conducted in the military in 1983. The price of VICEROY was reduced to near generic levels and while volume increased 366%, virtually none of that business came from generics. Therefore, B&W believes that branded generics will enhance the growth of the economy segment and will draw volume from popular priced brands. B&W believes that the black and white/private label generics will continue to be a large and viable

subsegment of the total economy segment. Black and white's have an established trade and consumer franchise which delivers substantial profits to the retailers. In addition, private label retailers, who have resisted black and white cigarettes, will continue to resist branded generics in order to protect their labels and profits. As a consequence, several strategic conclusions can be drawn.

1. *The economy segment has established itself in the U.S. market and will be a major part of the market in the foreseeable future.*

   U.S. consumers have demonstrated an increased propensity to smoke economy priced cigarettes and it is clear that to some smokers, price is more important than image. Further, while the financial penalty is severe, it is equally clear that two manufacturers find these margins acceptable, at least for the time being. (As a matter of perspective, the variable margins on generics today are better than those realized by the industry as recently as 1977.)

2. *A declining total market in combination with growth in the economy segment makes a strong competitive response inevitable.*

   The decline of the total industry and the four share points captured by generic/private labels have reduced the number of units to branded manufacturers by over 50 billion per year.

3. *The future shape of the Domestic U.S. market will change dramatically as a result of the emergence of the economy segment.*

   Cigarette manufacturers will either stay on the sidelines and accept the losses to economy offerings and attempt to limit future price increases in order not to fuel the growth of generics – or – they will enter the new segment in an attempt to participate in order to

manage prices and profitability upward. The latter appears to be the most predictable approach.

Private labels are expected to have a very long life cycle given the trade's interest in protecting its own brands. The long term staying power of black/white cigarettes is unknown but they are expected to be a significant factor in the near and intermediate term. It is quite likely that manufacturers will introduce branded generics, develop loyal franchises and then gradually raise prices over the longer term. Thus, the U.S. market could quickly become one of the multiple price tiers.

If the economy segment were to grow to 25 to 30 percent of the total market, manufacturers as a last resort may reduce list prices of full margin products in an attempt to repeat the action of the mid 1930's.

An additional impact could be reduced marketing support for full margin brands as manufacturers attempt to drive economy offerings and maintain bottom line profitability.

And finally, if all of this comes to pass, it could put in jeopardy a single focus strategy of full margin new products as the number of full margin brand smokers will decline as the economy segment grows.

4. *Brown & Williamson is the most vulnerable company to economy propositions.*

For the most part, B&W's portfolio of brands has a long history of decline (KOOL peak year – 1975, RALEIGH and VICEROY – 1966, BELAIR – 1969). The absence of inflows has resulted in an older and lower income franchise versus total smokers. It is these smokers that have been attracted to generics as outlined below.

Generic Smokers Indexed To Total Industry

Over 44	118
Less than $15,000	158

The contribution B&W has made to generics is significant and has been increasing.

B&W Contribution to Generics

		%	Fair Share Index
1981	1st Half	10.5	74
	2nd Half	12.9	91
1982	1st Half	15.6	115
	2nd Half	17.9	133
1983	1st Half	23.2	181
	2nd Half	20.2	170

It is our firm conviction that branded generics, which are heavily advertised and promoted (with both price and image benefits), will have an even more devastating impact on Brown & Williamson.

Projected Future Impact of Economy Segment

To fully understand the impact of the economy segment upon various manufacturers in the future, a projection has been made assuming that:

1. The economy segment grows to 10% of market by 1988. It was further assumed that two-thirds of this segment would be represented by black and white/private labels and one-third branded generics.
2. That each company would continue to contribute at their 1983 rate (B&W's fair share index remains at 170

for black and white/private label but increases to 200 for branded generics).

The following summarizes individual company volume losses versus expectation if no economic propositions had existed.

Projected Volume Loss To Economy Segment

(Billions)

	1984	1985	1986	1987	1988	Cume
B&W	6.6	9.5	10.4	11.5	12.5	50.5
RJR	11.9	17.1	18.9	20.9	22.6	91.4
ATC	2.2	3.1	3.5	3.8	4.1	16.7
PM	7.1	10.2	11.2	12.4	13.4	54.3
LOR	2.5	3.6	4.0	4.4	4.7	19.2
L&M	.8	1.2	1.4	1.6	1.8	6.8
Total Loss to Economy Segment	31.1	44.7	49.4	54.6	59.1	238.9
Economy Segment Share of Market	5.2%	7.5%	8.3%	9.2%	10.0%	

Even if these projections are off by 20%-30%, it is clear that the effect of the economy segment is significant for all manufacturers.

Competitive Responses

RJR has clearly stated its willingness to live with lower margins on volume *it otherwise would not have enjoyed*. If RJR is successful with Doral, a second branded entry should be anticipated. Irrespective of the success of Doral, if black and whites/private label continue to grow, RJR may well enter that segment too.

Philip Morris will probably take a 'wait and see' approach due to its less than fair share contribution to the growth of generics. If Doral is successful, Philip Morris will probably launch a branded generic.

Lorillard is expected initially to take a 'wait and see' approach, again due to its less than fair share contribution. Nevertheless, B&W believes that based upon a knowledge of the Lorillard management, that Lorillard will be the next company to enter this segment and would most likely reposition Old Gold at the generic price point (presently .3% share of market).

American is not expected to respond given its history of being the last in the industry to recognize new consumer trends.

L&M is expected to match RJR's discount structure and the military price point. In addition, L&M seems to be in an ideal position to launch a branded generic and could reposition Chesterfield at a lower price point (presently .5% share of market).

Brown & Williamson's Present Position

The 1984 Five Year Plan assumed some impact from the economy segment albeit at a far less significant level. Recasting the Plan numbers is necessary using the following assumptions:

1. The economy segment grows to 10% by 1988 split two-thirds black and whites/private label and one-third branded generic.
2. Brown & Williamson loses volume at a 170 fair share index to black and white/private label and at a 200 fair share index to branded generics.
3. All other assumptions remain as stated in the Plan.

Thus, if Brown & Williamson chooses to stay out of the economy segment, i.e., do nothing, it will suffer the following losses, based on the foregoing assumptions.

	1984	1985	1986	1987	1988	Cume
Share Loss	- .5	- .9	-1.0	-1.2	-1.3	
Volume Loss	-2.7	-5.4	-6.2	-7.0	-7.7	29.0
Trading Profit Loss	($29.5)	($65.3)	($82.2)	($101.0)	($120.2)	($398.2)

Brown & Williamson Alternative Strategies

1. *Utilize RICHLAND*

   A. *Convert RICHLAND 25's to 20's at Generic prices.*

   Advantages

   1. Some awareness and usage in 20% of U.S.

   Disadvantages

   1. Give up position in potential new segment.
   2. Smoker confusion in current 20% of U.S.
   3. No reason to believe RICHLAND better than other marks for economy segment.

   B. *Offer Richland 20's at Generic price in addition to current 25's offering.*

   Trade will not accept because of confusion in the market place.

2. *Convert established brand to generic price point.*

   Advantages

   1. Leverages existing awareness and heritage.
   2. Immediate national presence and large consumer franchise.
   3. Adds timing flexibility - could move now or later.

   Disadvantages

   1. Loss of significant trading profit.
   2. Branded generics may not succeed - uncertain about maintaining price point, and no

ability to recapture full margin consumer acceptance.

3. Reversal of declining trend doubtful.

Of B&W's established brands represents the one which has been focused on as a potential first entry as it would allow B&W to leverage existing awareness and heritage, provide national presence and a large group of current smokers.

REDACTED

This option is not recommended at this time. The major concern is the risk of $270MM of brand contribution over the Plan period, should the branded generic price point not be established broadly. In other words, should B&W drop the price and this not be reflected at retail, B&W will have succeeded in enhancing trade profitability without any resulting consumer benefit.

Nevertheless, this strategy will be readied for implementation in the event that the branded economy segment gains broad consumer acceptance and conversion of established brands to generic prices looks more viable.

3. *Enter Black and White/Private Label Part of Economy Segment*

Advantages

1. Potential for immediate volume improvement.
2. No investment spending.
3. Some profit contribution with potential for some margin improvement longer term.
4. Utilizes available production capability.

Disadvantages

1. Lack of brand ownership.
2. Shorter production runs.

4. *Introduce branded generic behind Doral*

Advantages

1. Takes advantage of RJR's leadership in establishing the price point.
2. Takes advantage of RJR's advertising and merchandising strategy.

Disadvantages

1. Not sure branded generic will succeed – with or without Doral. Uncertain about maintaining price point and distribution.
2. Draws from full margin smokers incremental.

Recommendation

The earlier concern of expanding the economy segment is no longer tenable, given RJR's recent action. It is clear that the economy segment is significant, and growing.

Accordingly, recognizing the importance of minimizing increased cannibalization and concomitant share erosion, as well as maintaining trade profit targets, it is imperative that B&W enter this segment. We propose the following program for entry:

1. Introduce a branded generic behind RJR and enter the black and white/private label segments nationally.

2. Limited marketing spending behind the branded generic relying on price and product quality as its consumer point of difference.

3. Take advantage of RJR's consumer advertising and merchandising to create awareness of branded generics.

4. Utilize an aggressive discount structure to obtain black and white/private label business.

5. Leverage the synergy of branded/black and white two-pronged approach by allowing branded generic sales to apply against the black and white discounts.

6. Longer term be prepared to reduce price on VICEROY if branded generics exhibit broad consumer appeal.

Marketing Approach

A. *Launch a full line of black and white* and private label styles:

   1. Same style array as L&M

   2. Same list price

   3. Superior discounts/allowances

   B&W will be prepared to spend full margin in order to displace Liggett & Myers as the trade source of generic and private labels, although not contributing, to trading profit, it will give us short term volume and share enhancement.

B. *Launch Hallmark at generic price*:

   Every successful new cigarette brand has achieved consumer acceptance because it has

offered a unique selling proposition. The level of success is primarily dependent upon the manufacturer's ability to generate awareness and trial – this in turn is a function of the willingness to invest marketing funds and realize near term losses.

In the case of Hallmark, the unique selling proposition is price. The weighted average retail price of B&W's offering will be *22% less* than *96% of all* cigarettes sold today.

Another key factor contributing to Hallmark's success will be RJR's efforts at establishing and maintaining the new price point – a feat B&W would have been unable to accomplish alone.

Further, RJR's merchandising program will create a new home for branded generics. This new home will be away from the popular priced brands and will communicate the new price structure to in-store consumers. Having a position on this fixture with appropriate point-of-sale materials, etc. will communicate the same price story for Hallmark.

In the product area and based on a very limited evaluation of Doral, the product appears to be a very low cost design. The product is unusual having nearly equal proportions of lamina, reconstituted, puffed tobacco and longer filters. The high level of puffed tobacco and longer filter result in low tobacco weights, ranging from 70-120 mg/cigarette less tobacco. The high level of reconstituted provides a vehicle for using larger amounts of scrap tobacco or offshore leaf. The quality of the lamina is not known.

The recommended Hallmark non-menthol product has tested at parity versus Winston, Century

Lights and generics. The Hallmark menthol product has scored parity versus Salem, Benson & Hedges Lights and, superior to generics. Therefore, we believe the smoking characteristics of Hallmark should be superior to those offered by Doral.

The marketing approach would encompass entering the same markets as Doral with identical style offerings. This would include lights products at 14mm tar, regular, menthol, king and 100's. The terms and allowances would replicate RJR's. B&W's program would also encompass a policy of no return goods.

B&W would invest a portion of available margin, buying shelf space on RJR's special Doral fixtures and on existing generic fixtures and some in-store merchandising support including shelf talkers, window banners and riser cards. The primary communication objective of all point-of-sale would be price and superior taste/quality would be the secondary objective. Forced trial via sampling, coupons, etc. would be executed on a targeted basis.

Since the B&W plan uses limited spending against what is believed to be the Doral approach, it is realized that the Hallmark share growth will be slow.

Such a recommendation will provide a strategic response to the following considerations.

1. Economy propositions are fulfilling a real consumer need as demonstrated by their continued growth and acceptance.

2. Entering black and white, private label and branded generics gives B&W a representation in all subsegments of the economy segment. The lack of entry leaves B&W out of a segment which may become more financially attractive over the long term.
3. B&W's concern over expanding the economy segment is no longer a barrier to entry. RJR's launch of Doral and the continued growth of the other subsegments require us to respond to minimize future losses.
4. Entry and success in this new segment will not impede B&W's ability to maintain its new product program.
5. Retailers will protect their vested interest in black and white/private labels and both are expected to remain on the market in the foreseeable future.
6. Both black and white and private label entries are required as they are merchandised through different retail customers.
7. Contrary to our previous position, introduction of a branded generic by B&W now appears to be feasible as RJR has the clout and sales force coverage to maintain the price on branded generics.
8. Not [sic] investment spending behind a branded generic is risky and will result in a lower growth rate, but is considered appropriate given B&W's need to husband resources for better margin new products.
9. An aggressive discount structure on black and whites/private labels will be required to get trade factors to switch manufacturers. Having gained the business, B&W believes that it will retain much of it as competitors will not be able to make their proposals meaningfully more attractive without selling below cost. Competitive response of this nature would be considered unlawful conduct.

10. Allowing B&W's branded generic sales to count toward black and white discounts overcomes a major trade problem with RJR's entry and will encourage acceptance and distribution.
11. The cost of entering the new segment is minimal. Entry, however, provides B&W with the potential for improving profitability through opportunistic pricing, either to lead or to follow as appropriate.
12. By nature of the Hallmark offering, timing is essential. Should a competitor preempt Brown & Williamson, then the Hallmark proposition, which is based on acquiring shelf space, is severely jeopardized.

Financial Implication of Recommendations

If B&W can successfully achieve a 60% participation by 1988 in the black and white generics segment, it has the opportunity, with minimal investment, under the pricing assumptions incorporated in our Plan, to recapture 23 billion units of volume by 1988, an increase in market share of 4 share points by 1988 and aggregate potential trading profit from 1984-88 of $342 million. This entry alone recoups the bulk of potential trading profit losses which could be expected by the virtue of a conscious decision to allow this segment to expand and be available to others. While it may require, to gain this business, the use of some or all of this potential trading profit, the expectation is that this segment can become more profitable, particularly as it approaches maturity.

In order to participate in the branded economy segment, B&W is recommending the introduction on a minimal investment basis of an economy brand, i.e., Hallmark

(This proposal assumes a certain cost for merchandising. If that cost is increased, then the proposal will be reappraised). If Hallmark achieves by 1988 a .6% share of market, a volume of some 3.6 billion units, B&W can anticipate, on assumptions consistent with those built into the Plan, to achieve trading profit of 30 million, in aggregate from 1984-1988, trading profit otherwise lost to competitors.

The combined strategy, then, of B&W entering the branded generic and the black and white/private label market, will over the five year period, based on the current forecasts, achieve both an incremental market share of 4.7%, and a volume of 27.3 billion in 1988. This enhances the probability of achieving the Plan trading profit.

LIFO Leaf Decrements

The impact of the proposed strategy on Plan LIFO Leaf decrements (in broad terms) is summarized in the following table:

LIFO Leaf Decrements
Dollars In Millions

	1984	1985	1986	1987	1988	Total 1984-1988
Plan Decrements	$11.2	$ 7.8	-	-	-	$19.0
Additional Decrements – Cannibalization	$ 9.0	$ 3.0	-	-	-	$12.0
Plan Decrements – Excluding New Products Beyond RICHLAND	$16.9	$21.0	$17.4	$17.2	$8.6	$81.1
Additional Decrements – Cannibalization	$ 9.0	$ 3.0	$ 2.0	$ 3.0	$4.0	$21.0
Decrements Over Five Year Period Assuming Proposed Strategy	$ -	$ -	$ -	$ -	$ -	$ -

As indicated in the table, incremental Plan LIFO Leaf decrements of $12.0 million would be experienced over the Plan period as a result of the incremental cannibalization and assuming B&W does not enter the economy segment.

If we assume B&W's non-entry and the absence of New Products beyond Richland, the incremental decrements over the Plan period from cannibalization become $21.0 million.

Entry into the economy segment under the assumptions included in the proposal would avoid Plan period decrements of $31.0 million (assuming successful New Product introductions) or by as much as $102.1 million (assuming no New Product introductions beyond Richland).

SUMMARY IMPACT ON FIVE YEAR PLAN DOMESTIC VOLUMES OF ECONOMY BRAND PROPOSAL

QUANTITIES IN BILLIONS

	*1984	1985	1986	1987	1988	TOTALS 1984-1988
Industry	583.5	596.8	594.9	593.3	590.7	
B&W Five Year Plan						
(Established Brands): Volume	64.7	62.6	59.1	55.7	52.6	294.7
: Share	11.1%	10.5%	9.9%	9.4%	8.9%	
Impact of Cannibalization						
on B&W: Volume	– 2.7	– 5.4	– 6.2	– 7.0	– 7.7	– 29.0
: Share	– .5%	– .9%	– 1.0%	– 1.2%	– 1.3%	
B&W Established Brands						
Post Cannibalization: Volume	62.0	57.2	52.9	48.7	44.9	265.7
: Share	10.6%	9.6%	8.9%	8.2%	7.6%	
Additional Volume						
– Black & White/Private Labels	2.2	15.2	21.1	22.8	23.8	85.1
Additional Volume						
– Hallmark	.3	1.4	2.3	3.2	3.5	10.7
Revised Established Brand Volume						
After Proposed Entry	64.5	73.8	76.3	74.7	72.2	361.5
Revised Established Brand Share						
After Proposed Entry	11.1%	12.4%	12.8%	12.6%	12.2%	

* 1984 B&W Plan Volumes have been reduced due to lower Industry expectations.

NOTE: The impact of the growth of the economy segment on New Products has not been quantified.

B. E. B.
5/14/84

mkh/2257

TRADING PROFIT OF ECONOMY BRAND PROPOSAL

DOLLARS IN MILLIONS

	*1984	1985	1986	1987	1988	TOTALS 1984-1988
B&W Five Year Plan Trading Profit	$416.1	$456.8	$496.0	$549.7	$608.9	$2,527.5
Impact of Economy Brand Cannibalization	– 29.5	– 65.3	– 82.2	–101.0	–120.2	– 398.2
B&W Trading Profit Post Cannibalization	$386.6	$391.5	$413.8	$448.7	$488.7	$2,129.3
Additional Trading Profit – Black & White/Private Label	$ 5.2	$ 43.6	$ 75.6	$ 98.4	$119.9	$ 342.7
Aditional Trading Profit – Hallmark	(1.3)	.4	5.2	11.2	15.0	30.5
Revised Trading Profit	$390.5	$435.5	$494.6	$558.3	$623.6	$2,502.5
Memo: Plan LIFO Decrement Avoided (Not Included)	$ 11.2	$ 7.8				$ 19.0
Memo: Plan Cannibalization Decrement Avoided (Not Included)	9.0	3.0				12.0
Total Decrement Avoided (Not Included)	$ 20.2	$ 10.8				$ 31.0

* 1984 B&W Plan Trading Profit has been reduced from $431.5 due to delay in RICHLAND launch and lower Established Brands volume as a result of lower Industry projection.

NOTE: The impact of the growth of the economy segment on New Products has not been quantified.

B. E. B.
5/14/84

2257/3

[Illegible]

IMPACT ON B&W'S FIVE-YEAR PLAN TRADING PROFIT OF GROWTH IN BRANDED GENERIC AND BLACK & WHITE/PRIVATE LABEL GENERIC CONTRIBUTING AT A 2.0X FACTOR AND 1.7X FACTOR RESPECTIVELY

(DOLLARS IN MILLIONS/QUANTITIES IN BILLIONS)

	1983 ACTUAL	*1984	1985	1986	1987	1988	TOTAL 1984-1988
Industry Estimate		583.5	596.8	594.9	593.3	590.7	
B&W Firm Plan Established Brands							
Share	11.5	11.1	10.5	9.9	9.4	8.9	
Volume	68.2	64.7	62.6	59.1	55.7	52.6	
Generics							
Branded	–	2.3	12.5	14.3	16.6	19.5	
Black & White/Private Label	17.4	28.8	32.2	35.1	38.0	39.6	
Total Volume	17.4	31.1	44.7	49.4	54.6	59.1	
Year-To-Year Volume Change		+13.7	+13.6	+ 4.7	+ 5.2	+ 4.5	
Impact of Cannibalization on B&W @ 2.0X for Branded and 1.7X for Black & White/Private Label							
Volume							
Volume Cannibalized		– 2.7	– 5.4	– 6.2	– 7.0	– 7.7	–29.0
Adjusted Volume		63.7	57.2	52.9	48.7	44.9	
Adjusted Share		10.6	9.6	8.9	8.2	7.6	
Trading Profit Impact							
Variable Margin		$(38.7)	$(85.0)	$(106.2)	$(130.0)	$(154.3)	$(514.2)
Marketing Spend		5.9	12.6	15.3	18.5	21.5	73.8
Manufacturing Overheads		1.4	2.9	3.5	4.1	4.9	16.8
Profit Sharing		1.9	4.2	5.2	6.4	7.7	25.4
Trading Profit		$(29.5)	$(65.3)	$ (82.2)	$(101.0)	$(120.2)	$(398.2)

* 1984 B&W Plan Volumes have been reduced due to lower Industry expectations.

NOTE: The impact of the growth of the economy segment on New Products has not been quantified.

T. W. W.
5/14/84

DISK 91

TRADING PROFIT EFFECT
OF B & W ENTERING GENERIC MARKET
BLACK AND WHITE/PRIVATE LABELS

	1984	1985	1986	1987	1988	TOTAL
VOLUME	2.2*	15.2*	21.1*	22.**	23.**	*5.1*
SALES REVENUE	41,492	3**,96*	441,623	5*4,336	5**,492	1,843,9*3
RATE PER M	1*.86	19.**	2*.93	22.12	23.34	21.67
VARIABLE COST	(31,262)	(221,464)	(314,6*1)	(34*,612)	(373,66*)	(1,289,599)
RATE PER M	14.21	14.57	14.91	15.29	15.7*	15.15
VARIABLE MARGIN	1*,23*	79,496	127,*22	155,724	181,832	5*4,3*4
RATE PER M	4.65	5.23	6.*2	6.83	7.64	6.51
TRADE ALLOWANCES	(3,63*)	(25,***)	(34,*15)	(37,62*)	(39,27*)	(14*,415)
RATE PER M	1.65	1.65	1.65	1.6*	1.65	1.65
BRAND CONTRIBUTION/(LOSS)	6,6**	54,416	*2,2*7	118,1*4	142,562	413,**9
RATE PER M	3.**	3.5*	4.37	5.18	5.99	4.86
INCREMENTAL OVERHEAD	(1,1**)	(*,***)	(11,*16)	(13,452)	(14,994)	(49,418)
RATE PER M	*.5*	*.53	*.56	*.59	*.63	*.58
PROFIT SHARING	(33*)	(2,782)	(4,*23)	(6,279)	(7,6*4)	(21,***)
RESERVE FOR TRADING PROFIT OR ADDITIONAL TRADE ALLOWANCES	(5,17*)	(43,57*)	(75,*6*)	(98,373)	(119,914)	(342,6*3)
RATE PER M	2.35	2.*7	3.5*	4.31	5.**	4.*3
TRADING PROFIT	(*)	(*)	(*)	(*)	(*)	(*)

• Sales Revenue: 1984 – Assumes no additional increase in 1984 from current 5/3/84 prices.

1985 and Forward – Assumes the same net price relationship of Generic to full priced products that exist at present (65% of full priced).

• Variable Cost – Assumes *no* manufacturing cost improvements due to specification changes, etc.

• Trade Allowances – Were assumed to be the same as used in the February proposition.

[* = Illegible]

TRADING PROFIT EFFECT OF B&W ENTERING GENERIC MARKET HALLMARK

(Dollars In Thousands)

	1984	1985	1986	1987	1988	TOTALS
Volume (Billions)	.30	1.40	2.30	3.20	3.50	10.70
Sales Revenue	5,589	27,370	47,518	69,888	80,640	231,005
Rate Per M	18.63	19.55	20.66	21.84	23.04	21.59
Variable Cost	(4,263)	(20,398)	(34,293)	(48,928)	(54,950)	(162,832)
Rate per M	14.21	14.57	14.91	15.29	15.70	15.22
Variable Margin	1,326	6,972	13,225	20,960	25,690	68,173
Rate per M	4.42	4.98	5.75	6.55	7.34	6.37
Introductory Allowance	(78)	(122)	–	–	–	(200)
Distribution Allowance	(130)	(677)	(1,193)	(1,652)	(1,805)	(5,457)
Merchandising Support	(2,300)	(5,000)	(5,240)	(5,494)	(5,764)	(23,798)
Rate per M (Total Marketing)	8.36	4.14	2.80	2.23	2.16	2.75
Brand Contribution/(Loss)	(1,182)	1,173	6,792	13,814	18,121	38,718
Rate per M	(3.94)	.84	2.95	4.32	5.18	3.62
Incremental Overhead	(150)	(742)	(1,288)	(1,888)	(2,205)	(6,273)
Rate per M	.50	.53	.56	.59	.63	.59
Profit Sharing	80	(26)	(330)	(716)	(955)	(1,947)
Trading Profit/(Loss)	(1,252)	405	5,174	11,210	14,961	30,498

Selling Prices – will be the same as Generic (Black & White) prices, however, discount terms will be 3¼ rather than 2% allowed on Generic.

Variable Cost – Assumes no manufacturing Cost improvements (same as Black & White)

Introductory Discount Allowance – Assumes $9.60 per 12M case (.80 per M) on the first month sales.

Distribution Incentive Program

1984 – .48
1985 – .49 weighted
1986-1988 – .51

Merchandising Support – Has been included at $5,000 in 1985, increased in the forward years for inflation.

B. E. B.
5/12/84

2257/2

SUMMARY
IMPACT ON B&W'S FIVE-YEAR PLAN TRADING PROFIT OF GROWTH IN GENERICS WITH B&W NOT PARTICIPATING AND B&W CONTRIBUTING AT A 1.0X FACTOR

(DOLLARS IN MILLIONS/QUANTITIES IN BILLIONS)

	1983 ACTUAL	*1984	1985	1986	1987	1988	TOTAL 1984-1988
Industry Estimate		583.5	596.8	594.9	593.3	590.7	
B&W Firm Plan Established Brands							
Share	11.5	11.1	10.5	9.9	9.4	8.9	
Volume	68.2	64.7	62.6	59.1	55.7	52.6	
Generics							
Branded	–	2.3	12.5	14.3	16.6	19.5	
Black & White	17.4	28.8	32.2	35.1	38.0	39.6	
Total	17.4	31.1	44.7	49.4	54.6	59.1	
Year-To-Year Volume Change		+13.7	+13.6	+ 4.7	+ 5.2	+ 4.5	
Impact of Cannibalization @ Fair Share							
Volume Cannibalization		– 1.5	– 2.9	– 3.3	– 3.8	– 4.2	–15.7
Adjusted Volume		64.9	59.7	55.8	51.9	48.4	
Adjusted Share		10.8	10.0	9.4	8.7	8.2	
Trading Profit Impact							
Variable Margin		$(21.5)	$(45.6)	$(56.5)	$(70.6)	$(84.2)	$(278.4)
Market Spend		3.3	6.8	8.1	10.0	11.7	39.9
Manufacturing Overheads		.8	1.5	1.8	2.2	2.6	8.9
Profit Sharing		1.0	2.2	2.8	3.5	4.2	13.7
Trading Profit		$(16.4)	$(35.1)	$ (43.8)	$(54.9)	$(65.7)	$(215.9)

* 1984 B&W Plan Volumes have been reduced due to lower Industry expectations.

NOTE: The impact of the growth of the economy segment on New Products has not been quantified.

T. W. W.
5/14/84

2255/7

BRAND CONTRIBUTION

(1984 ESTIMATED; 1985-1988 FIVE YEAR PLAN)

(Dollars In Millions)

PLAN	1984	1985	1986	1987	1988	TOTAL 1984-1988
Volume (Millions)	6,400	5,946	5,385	4,861	4,386	26,978
Margin	$ 93.9	$ 94.2	$ 92.1	$ 89.8	$ 87.5	$ 457.5
Rate per M	14.67	15.84	17.11	18.48	19.96	
Marketing Spend	11.1	10.9	10.4	9.9	9.4	51.7
Brand Contribution	$ 82.8	$ 83.3	$ 81.7	$ 79.9	$ 78.1	$405.8

IMPACT ON CONTRIBUTION – CONVERTING TO BRANDED GENERIC

	JULY-DEC.	1985	1986	1987	1988	TOTAL 1984-1988
Volume (Millions)	3,283	5,946	5,385	4,861	4,386	23,861
Margin Lost	$–32.4	$–63.1	$–61.0	$–58.1	$–55.4	$– 270.0
Volume required to breakeven – approximately 3.0X						
Memo Data:						
Selling Price Differential Per M						
Full Price	$28.49	$30.26	$31.98	$33.80	$35.67	
Doral Price	18.63	19.65	20.66	21.84	23.04	
	$ 9.86	$10.61	$11.32	$11.96	$12.63	

T. W. W.
5/14/84

mkh/2259

REDACTED

MEMORANDUM

TO: L. W. BUTLER
D. P. CHRISTENSEN
C. C. MIDDLETON
A. E. ROZEK
D. J. BORES
J. K. THARALDSON
G. E. GREENIER

FROM: T. A. OLGES

SUBJECT: *DOMESTIC COMPETITIVE ANALYSIS*

DATE: MAY 15, 1984

Enclosed is your personal copy of the Domestic Competitive Analysis May 1984 Update. The intent of this document is to provide Brown & Williamson management a better understanding of our major competitors' total businesses.

However, care should be exercised in the circulation and safe retention of this *"RESTRICTED"* document. The Domestic Competitive Analysis Update is for internal use only and no additional unauthorized copies should be made.

If you have any suggestions or comments concerning this document, please feel free to contact me.

/s/ Trina Olges
T. A. Olges

Enclosure

/mjs/2021J

* * *

Brand	Characteristics	Dates	Other
Oasis	Filter, 85mm, menthol flavor only (no regular)	Withdrawn 1983	
Scotch Buy	Filter, 85mm, reg. & Menthol flavor, low tar, soft pack, filter, 100mm, reg. flavor, low tar, soft pack; filter, 85mm, reg. ultra low, soft	Advertised in Washington, DC in Summer 1983	Private label brand for Safeway supermkts lights=14 mg. tar, 1.1 mg. nicotine; ultra lights=6 mg. tar, 0.7 mg. nicotine advertised at $6.99 per carton

3. *Creative*

L&M has run very little advertising in the past several years. Most of their recent growth has come from slightly advertised styles – generics. They continue to run well-targeted fractional page units to support Eve.

4. *Gaps in Brand Portfolio* (Reference Appendixes 5, 6 and 7)

L&M remained strong in the Plains, 120mm and Slims segments based on a slight increase in Eve and continued lack of activity in the Plains segment.

L&M's Light segment share continues to improve through the strong performance of Generic Light Kings, 100s, Menthol Kings and Menthol 100s.

L&M's 1982 portfolio gap in the Ultra Light segment (FSI=17) was substantially filled (FSI=70) with the recent introduction of Generic line extensions – Ultra lights Non-Menthol and Menthol Kings and 100s. With strong generic performance in 1984, L&M is estimated to achieve a relatively balanced portfolio, with remaining gaps in only the full taste and box categories.

L&M's future rests on generics growth, as it is L&M's only large brand, it must generate both growth and funds for L&M.

	Brand	Growing '83 Share	'83 Growth	Brand	Declining '83 Share	'83 Growth
Large: (SOM > 2)	Generic	2.9	67.5%	None		
Small: (SOM < 2)	Eve	.4	27.0	L&M	.7	-11.9%
				Lark	.4	- 5.7

* * *

III. GENERIC COMPETITION

Recent Trends

The dramatic success of Liggett and Myers' generic/private label cigarettes has been a major concern for the cigarette manufacturers. In little more than four years, generic sales have grown to 4% of all Domestic cigarette sales. However, this growth in share has been a recent phenomenon. During the first two years of national introduction, generic cigarettes commanded little attention in the marketplace and reached less than .5%. For 1982, share grew to .9% and in 1983 spurted to 2.9%. For year-end 1984, some analysts estimate the generic share as high as 4.5-5%.

Short-Term Forecast

With the continued growth of generic cigarettes as with many other generic products, their success appears more than a temporary trend. Although the inflationary price structure caused by the Federal Excise tax increase and the U.S. recession fueled the products' quick growth, L&M's actions including introduction of a broad product line, increased distribution, private label manufacture, good wholesaler/retailer margins, long-term contracts and quality products have insured that these products will become a permanent category in the marketplace. L&M's strategies have made generic cigarettes a legitimate alternative, recession or not, for a certain number of smokers. However, the question of the ultimate size of this segment long-term remains. Some analysts view generic growth as peaking in 1984. Others in the industry anticipate continued further generic growth, though at a substantially slower rate, and that the segment will grow potentially becoming 7% or more of the market.

Competitive Activity

Generic growth represents volume erosion for all competitors. Unchallenged, L&M will continue aggressive segment development since it has virtually no stake in the branded, full price market.

1983 Losses to Generics
(Total Generic Volume of 17.48 Sticks in 1983)

	Contribution to Generics* %	Fair Share Loss Index	Volume Loss (BB Sticks)	Variable Margin Loss** ($MM)
American	7.0	(83)	1.28	16.3
Brown & Williamson	21.1	(170)	3.78	48.2
Liggett & Myers	3.0	(120)***	.58	7.4
Lorillard	8.0	(83)	1.48	18.9
Philip Morris	22.7	(73)	3.98	50.7
R. J. Reynolds	38.2	(118)	6.78	86.4

*Based on Switching Study, Waves 34 and 35
**Assumes $12.75/M variable margin
***Excluding generics

While Brown & Williamson had the highest loss relative to fair share, generics had the greatest volume and profit impact on R. J. Reynolds.

By company, we hypothesize the following anticipated competitive actions:

1. *R. J. Reynolds*

   In terms of total volume and variable margin lost to generics, RJR is the most vulnerable company now and in the future.

   Further, RJR has no brand currently able to replace these lost sales; no established RJR brand grew in 1983. Barring a major new brand success (Sterling or other) or an unforeseen turnaround of an existing brand(s), RJR must assault the economy segment to hold share and volume. In response to generics, RJR will pursue one or more of the following strategies:

   Priority One

   Launch a generic product line to gain control of and contain generic segment growth. RJR would strive to limit segment development since incremental generic growth will disproportionately reduce RJR's total margins.

   During early April 1984, the *Chicago Tribune* reported that RJR was ready to relaunch the Doral brand as a generic and late in April RJR announced Doral as such in a 13-state test market.

   Priority Two

   Launch a mid-priced brand. This is RJR's second best option to gain volume given its sales force size and strength, domination and control of retail display fixtures and available list of low volume brands. These resources position RJR to distribute and sustain a mid-price at retail.

   Priority Three

   Increased discounting of RJR's full line of branded products in an attempt to reduce outflows to generics.

   Priority Four

   Continue and intensify development of the 25's segment.

   While RJR may pursue this strategy, the source of business for 25's is currently branded, not generic products. Increased support of 25's does not therefore represent a direct, effective defense against generics' growth.

[Handwritten margin notes illegible]

LIMITED

MEMORANDUM

May 17, 1984

[Handwritten Note]
Posey Jones
To All
Meetings

TO: R. A. BLOTT

cc: L. W. Butler
D. I. Falk

FROM: [Crossed Out]

SUBJECT: *PROJECT VOLUME – STATUS*

Doug and I have been pushing the "peanut" forward in anticipation of a positive decision. Within reasonable limits, certain department heads have been brought up to speed so that we can respond quickly if London approves Project "V" introduction.

The following is a summary of current "knowns":

Generics

1.) *Tactical Selling Plan*

Attached is a copy of our tactical plan; it will serve two purposes. First, it will be used as the core document for internal operational decisions once you form the implementation task force. Secondly, it contains a revised volume discount structure (page 4) and priority customer "hit list" (page 5).

This document also contains the Heartland Tobacco Company's organizational chart. A full-time exempt staff of seven people is planned. I have recommendations ready for the six selling managers and am working with Jerry Grasch to identify candidates for the Marketing Services position. I want to activate this position as soon as we have a green light.

The final page of this attachment outlines sales territory boundaries fashioned along state lines so that we can compete effectively against current generic volume. No more than two relocations will be necessary. The attached document details are current thinking in regard to clerical support for the six selling managers.

2.) *Packaging*

Doug is in the process of completing finished art. Silk screen or litho labels will be used for the production of initial selling samples.

* * *

5. Negotiated Services

   a. Returned goods – Heartland Tobacco will accept returned goods through B&W from all customers for the purpose of preparing and forwarding affidavits for reimbursement of tax stamps. If a customer insists on credit for returns, five cents will be deducted from his per carton volume discount. (B&W to keep Federal tax reimbursement.)

   b. Retail services beyond initial launch – If these are requested, Heartland Tobacco will provide a quarterly merchandising/inventory control service at a cost to the customer of one cent deducted from his per carton volume discount.

   c. Co-op advertising – No allowance will be provided, but advertising slicks will be made available to customers free of charge.

C. Target Customer List

The following customers will be presented with the initial program offering by the assigned B&W selling managers, as indicated. The Key Accounts Managers currently responsible for these accounts may be called upon to assist as needed.

Customer	Selling Manager
Core-Mark Trade Development A. M. Lewis	L. W. Butler
Generic Products Corp. Bosart Co. Seneco Revco Federated Foods, Inc.*	D. P. Christensen
Fleming Foods	G. A. Greenier
McLane Malone & Hyde	H. E. Higgins
Old Dominion Thomas & Howard	F. J. Schoenheiter
Wetterau	G. A. Korfhage

*Probable supplier for Thomas & Howard (a broker similar to Generic Products Corp.)

The above list represents the 14 largest direct customers with respect to "black and white" generics volume potential (exceptions: Core-Mark and Revco private labels, both of which are primarily "black and white"). B&W will match each customer's current generics label as closely as possible to facilitate consumer acceptance.

[Handwritten Note]

Dick:

Still under debate. We are not prepared to make a firm recommendation yet.

Don C.

(Note: Those customers with retail outlets in the 14-state HALLMARK test area will be offered both HALLMARK and generic brand styles as a "package deal," with cumulative volume for both brands determining the customer's volume discount bracket. See HALLMARK plan for incremental cost of this option.)

D. Retail Point Of Sale

The following fixture/P.O.S. materials will be provided out of each customer's 7¢ per-carton allowance:

1. Permanent displays

   a. Cartons – Separate permanent carton fixtures will be drop-shipped to retail outlets upon receipt of store list from customer.

   b. Packages – Space will be provided on the top shelf of the permanent carton fixture and/or on separate counter displays. Counter displays will be shipped to the customer's warehouse for distribution to retail outlets.

* * *

ATTACHMENT I

POSSIBLE COMPETITIVE REACTIONS AND B&W'S RESPONSES

A. L&M will be forced to address three pressure points applied by B&W's initial offer:

1. *Chain/Distributor Volume/Growth Discount Differential* – L&M currently offers distributors a lower volume and "growth" discount incentive than they do chains. B&W's offer exceeds L&M's chain offer and is unilateral.

2. *Volume Brackets* – L&M does not offer additional discounts to customers with volumes greater than 500 cases quarterly. B&W's volume discount structure includes two brackets above this volume level.

3. *Advertising Allowance* – L&M currently offers a \$.02-\$.12 per carton allowance for co-op advertising. A probable reaction at some point during the negotiating process will be to drop this allowance and transfer these funds into their volume discount structure.

B. B&W's Reactions

1. If L&M increases its discount offering, B&W will match the increase and raise the offer by an equal amount.

2. If L&M's offer approaches B&W's full variable margin, B&W will withdraw its seven-cent-per-carton fixture/P.O.S. allowance and be prepared to offer a discount structure equal to full variable margin in the highest volume bracket.

3. If L&M reduces list price, B&W will respond with a comparable increase in volume discount structure. (A reduction in list price by L&M is highly unlikely due to the resulting reduction of wholesaler profits in fair-trade states.)

4. If L&M offers returned goods credit at net list, B&W will offer customers a choice of:

   a) an additional five cent-per-carton discount *or*

   b) returned goods credit at net list.

5. If L&M increases its sales force support, B&W will offer customers a choice of:

   a) an additional one cent-per-carton discount *or*

   b) quarterly merchandising/inventory management service.

6. If L&M expands its generics product line to include full-flavor styles, B&W is prepared to match the offer style for style.

/ds644T

COPY TO:
WLS
JAF
"LIMITED"

NOTES ON PROJECT VOLUME TASK FORCE MEETING, TUESDAY, MAY 22, 1984

D. Christensen)
D. Falk) Presented
J. Tharaldson)

Project Volume is official. Customer contacts to begin either May 24 or 29.

Heartland Tobacco Co. is the shell company established.

A synopsis of L&M (Gary Tobacco) generic cigarette business follows.

A. *Two offers:*
   (1) *Chains*
   - List price higher than Dist.
   - Volume discount 10-20¢ per carton rebated quarterly based on actual volume.

   (2) *Distributors*
   - List Lower
   - Volume discount 3-15¢ carton

B. *Cooperative Advertising* – 3-12¢ discount per carton set in an escrow account based on performance – i.e. ads demonstrate certain activity level.

C. *Fixture & Display Escrow* – Regardless of volume 7¢ a carton – not on chains.

B&W Program – (Heartland Tob.)

Objective of program is to regain market share and to fill plant capacity – not going into it with the objective to make a profit.

Major thrust is to sell to our 14 top customers.

Four lines of products offered.

(1) Filter | Largest dist. offered choice of

(2) Blended | the three – next largest two

(3) Branded | remaining – next largest – remainder

(4) Branded Filter – intent to sell to GPC

Three major volume accounts in each state – Control by account/state basis.

No cooperative advertising allowance. Only one offer – one list price – will match L&M's list price.

Terms 2/10, net 14

Volume discounts (proposed)

Quarterly:	≥	1,500 cases	30¢ ctn.
	≥	1,000 cases	25¢ ctn.
	≥	500 cases	20¢ ctn.
	≥	200 cases	15¢ ctn.
	≥	100 cases	10¢ ctn.
	<	100 cases	List

Up front credit memorandum or check at end of quarter.

Fixtures and displays supplied free – in-house escrow account of 7¢ carton.

B&W will be willing to negotiate the volume discount up to our full variable margin – 85¢ per carton.

Expect initial orders to trickle in due to the fact that it will initially be a process of replacing product already in customers' warehouses – full impact may not be felt until October, 1984.

May 24 – Sales call begin
July 10 – Manufacture begins (may be during shutdown week)
July 24 – First shipment to distributors

After the 14 major customer contacts are made – formalize offer to trade. Offers to trade – negotiated.

Concerns of trade besides price is *service* and quality of product.

B&W fully expects L&M to file suit and to fight price competitively.

CLAUDIA H. KELLEY

05/22/84

/cjs

[Handwritten Note]

Carried by IWH to CIM
in response to BATUS position
that we must show profit

LIMITED

TRADING PROFIT EFFECT OF LAUNCHING BLACK AND WHITE/PRIVATE LABEL CIGARETTES

In order to displace Liggett & Myers as the trade source of black and white/private label generics, B&W is planning to offer the trade attractive discounts to gain this business.

As indicated on the attached financial schedule, B&W has allowed in the aggregate $1.65 per M in trade allowances which will vary by customer, depending on the profile of the customer and the volume of business attained.

While B&W does not intend to offer on average more than $1.65 per M in trade allowances, very large customers may exceed this amount modestly. Therefore, all of the business will yield a favorable trading profit of approximately $2.35 per M.

Anticipating the L&M will take an aggressive posture in discounting to protect this business, B&W is prepared to counter by increasing trade allowances in the aggregate by an additional $1.35 per M, which will still leave a trading profit of $1.00 per M overall and assure this business will be marginally profitable.

Copy given JAL✓
EPT
TWN

PGB

C.J. HEGER/af
5/22/84

TRADING PROFIT EFFECT
OF B & W ENTERING GENERIC MARKET
BLACK AND WHITE/PRIVATE LABELS

	1984	1985	1986	1987	1988	TOTAL
VOLUME	2.2*	15.2*	21.1*	22.**	23.**	85.1*
SALES REVENUE	41,492	3**,96*	441,623	5*4,336	***,4*2	1,843,9*3
RATE PER M	1*.86	**.**	2*.93	22.12	?3.34	21.*7
VARIABLE COST	(31,262)	(221,464)	(314,6*1)	(348,612)	(373,66*)	(1,289,599)
RATE PER M	14.21	14.57	14.91	15.29	15.7*	15.15
VARIABLE MARGIN	1*,23*	7*,496	127,*22	15*,724	181,832	554,3*4
RATE PER M	4.65	5.23	6.*2	6.83	7.*4	6.51
TRADE ALLOWANCES	(3,63*)	(25,***)	(34,*15)	(97,62*)	(39,278)	(14*,415)
RATE PER M	1.65	1.65	1.65	1.65	1.65	1.65
BRAND CONTRIBUTION/(LOSS)	*,***	54,416	92,2*7	118,1*4	142,562	413,*89
RATE PER M	*.**	3.58	4.37	5.18	5.99	4.86
INCREMENTAL OVERHEAD	(*,***)	(8,*56)	(11,816)	(13,452)	(14,994)	(49,418)
RATE PER M	*.5*	*.53	*.56	*.59	*.*3	*.*8
PROFIT SHARING	(3**)	(2,7**)	(4,*23)	(6,279)	(7,6*4)	(21,*68)
RESERVE FOR TRADING PROFIT OR ADDITIONAL TRADE ALLOWANCES	(5,17*)	(43,57*)	(75,56*)	(9*,373)	(119,914)	(342,6*3)
RATE PER M	2.35	2.*7	3.5*	4.31	5.*4	4.*3
TRADING PROFIT	(*)	*	(*)	(*)	(*)	(*)

• Sales Revenue: 1984 – Assumes no additional increase in 1984 from current 5/3/84 prices.

1985 and Forward – Assumes the same net price relationship of Generic to full priced products that exist at present (65% of full priced).

• Variable Cost – Assumes *no* manufacturing cost improvements due to specification changes, etc.

• Trade Allowances – Were assumed to be the same as used in the February proposition.

[* = Illegible]

[In Evidence 6/4/84]

HEARTLAND TOBACCO COMPANY

B&W (HEARTLAND)

GENERIC CIGARETTES

* * *

DIRECT ACCOUNT INFORMATION – (FOR FIELD USE ONLY)

First Ship Date:	July 17, 1984 (NOTE: Although we will be in a position to make shipments on July 17, we may be under some manufacturing constraints during this first week; therefore, take this into consideration when placing your orders.)
List Price	$18.75 per M – Kings $19.75 per M – 100's
Terms:	
Introductory	2%, 30 days received; net 31 mailed. Introductory terms will be available on all Heartland products pruchased and shipped on or before September 30, 1984.
Regular	2%, 14 days received; net 15 days mailed

CONFIDENTIAL

Trade Allowances:

Quarterly Case Volume Commitment	Per Carton Allowance
1,500 +	30¢
1,000 - 1,499	25¢
500 - 999	20¢
200 - 499	15¢
100 - 199	10¢

Volume rebates will be accumulated on a quarterly basis and a check will be issued from the Home Office based on actual purchases.

We believe Heartland's Trade Incentive offer is a significantly better buy for our customers. Let's compare based on the feedback we're [sic] received from various Field Sales Force personnel.

Competitive Generic
Incentive Plan

Cases Per Qtr.	Per Carton Rebate
100 - 199	0
200 - 249	0
250 - 499	10¢
500 - 999	13¢
1,000 - 1,499	13¢
1,500 +	13¢

Heartland's
Generic Incentive Plan

Cases Per Qtr.	Per Carton Rebate
100 - 199	10¢
200 - 249	15¢
250 - 499	15¢
500 - 999	20¢
1,000 - 1,499	25¢
1,500 +	30¢

- Our Volume Rebate Plan is the same for distributors and direct chains.
- Our Volume Rebate Plan covers cases sold from 100 – 250 cases per quarter. The competitor's incentive program does not.
- We offer additional volume rebates to customers with volume greater than 500 cases per quarter. The competitor's incentive program does not.
- Heartland will pay on the amount of product purchased, not necessarily the contracted amount. For example, if an account contracted for 900 cases at a 20¢ per carton rebate, but actually purchased 1,000 cases, which is at a 25¢ per carton rate, he would receive the 25¢ per carton rebate on the entire 1,000 cases.
- Although the competitor offers a periodic advertising allowance between 2¢ and 12¢ per carton quarterly, keep in mind the customer must pay for the advertising out of this amount. Therefore, the net amount is substantially less. We will provide "ad slicks", free of charge, if the account requests them.
- Customers currently pay shipping and handling for their generic fixtures, or receive them free of charge through special programs and promotions. Heartland will provide fixtures at *no cost*.

In summary, even when all these competitive optional payments are added together, our program is by far more profitable.

Allocation:

Generic cigarettes will not be under allocation.

Refer to Submitting Orders Section for complete details concerning ordering the product.

Returned Goods:

Credits will not be issued to customers for the list price of returned goods. In addition, no handling allowance payment will be made.

Heartland will, however, pay the shipping cost and accept returns for the reimbursement of applicable federal excise taxes and preparing affidavits covering the reimbursement of state and local excise tax.

A special form is being designed for this purpose. In the event you need to return any Heartland Generics before you receive this new form, call Sandee Nielander in the Sales Order Department. Do not combine Generics with regular B&W products on the normal #SA-65.

ADVERTISING AND CONSUMER INCENTIVES

No media advertising is planned at this time. Heartland, however, will provide "ad slicks", free of charge, to accounts if they wish to place advertisements.

Samples of ad slicks will be sent to you in the near future.

No consumer incentive offers are planned at this time.

June 13, 1984

MEMORANDUM

TO: Didi Hunt

cc: Don Fish
Steve Price
Nancy Rehling
Marianne Zen[Illegible]

FROM: Cindy Avery

RE: *Q SEAL PROGRAM*

This forwards a recap of sequential events leading up to development/launch of the Generics Q Seal:

BACKGROUND

Concept of Q Seal initiated by Jim Dowd as potential means of preventing competitive inroads into Generic segment. (Initial correspondence 4/28/82; project tabled by Jim due to price increase opportunity until Fall '83)

Secondary purpose of Q Seal was to reinforce quality among consumers (although it was recognized building awareness of Q Seal Concept would be long term endeavor).

EVENTS

1) Development original objectives/strategies for Q Seal program – (December 1982)

2) Q Seal Concept Research (February 1983)

   - proposal, summary, final report enclosed

- next steps were to take three viable concepts and refine design/color alternatives

3) Seal Alternatives mocked up. Gold Q Seal was recommended because it complimented all Generic/private label packages.

   Decision to proceed with Gold Q Seal made by Jim/Agency - 4/12/83, see enclosed project plan

4) Agency developed test market plan, enclosed

   - original 2/22/83
   - revised 4/13/83
   - August launch

5) Century launch triggered request for evaluation of Q Seal test market v. national introduction, enclosed. Agency recommendation to test market was based on concerns that sales force would not be available for national execution of merchandising/point-of-sale.

6) Decision made to go national by Jim; timetable for national launch same as for test market. Artwork for final Q Seal initiated.

7) Sell-in of Q Seal Concept initiated June/July '83 with prototypes of Q Seal. First shipment of product with Seal believed to have occurred August/September 1983.

8) Sales presentation/correspondence to Mike/Roy, enclosed. Sales meeting - September 1983.

9) Q Seal Tracking Study proposal developed/approved 8/27/83.

10) Q Seal Media plan developed/approved/targeted for October implementation.

11) Advertising Program (Nov. 1983 - Jan. 1983)

12) Follow-up

   - Tracking Study implemented/results presented 4/84
   - Q Seal sponsorship of World's Fair
   - Use of Q Seal visual in all advertising/point-of-sale.

We are in the process of developing a proposal which demonstrates how Q Seal can be used to thwart the introduction of generic cigarettes by B & W. We will be in touch to discuss this further.

CA/cg
Enclosures

[Handwritten Notes]

Carol P. Jova

Steve –

Thought you'd find this interesting – result of our sending the B&W lawsuit news release to customers.

I will send him a note thanking him for sharing the info, etc.

Carol

CITY SALES
INC.

WHOLESALE DISTRIBUTORS
Tobacco, Candy, Sundries

524 W. Chicago Avenue,
East Chicago, IN 46321 (219) 397-9040 • (800) [Illegible]

Heartland Tobacco Company
Vice President – Sales
1500 Brown Williamson Tower
Post Office Box 35090
Louisville, Kentucky 40232

June 22, 1984

Sir,

Please accept this as written notification to cancel our "AGREEMENT" and "ORDERS" of Generic cigarettes sold by Heartland Tobacco Co.

After careful consideration we decided not to carry your "brand" of Generics. We feel additional "brands" of

Generic cigarettes added into an established Generic market could lead to the demise of that market.

1. Smokers smoke brands because of "TASTE." Since your blend is different, the smoker will have difficulty identifying the brand he/she can count on supplying them with the "taste" they like, hence, dissatisfaction.

2. Similar packages will lead to the confusion where retailers retain more than one brand of Generic cigarettes.

3. Similar packages will lead to picking confusion and errors by distributors who are almost forced to carry all brands of cigarettes.

4. This "brand" would lead to larger inventories and lower turns of inventory at the distributor level because of competing Generic "brands"

5. Finally, no better deal is being offered as incentive to make a troublesome addition to our inventory. With that we feel there is little hope your "brand" will displace the one we currently use.

Respectfully,

/s/ R. J. Skurka
Robert J. Skurka
Vice President
Sales & Marketing

/s/ Stanley F. Skawinski Jr.
Stanley F. Skawinski Jr.
Vice President
Operations

[Handwritten Note]

Carol,

Thanks for the good news contained in your newsletter dated 2 July '84. You may be interested in our opinion.

Bob Skurka

NEWSNEWSNEWSNEWS
Liggett & Myers Tobacco Company, Inc., Durham, N.C.

[Handwritten Note]

Rec'd from Bert Trompeter
7/6/84

FOR IMMEDIATE RELEASE
CONTACT: CAROL JOVA 919-683-8992 JULY 2, 1984

Liggett & Myers Files Suit Against Brown & Williamson

Today, Liggett Group Inc. filed suit against Brown & Williamson Tobacco Corporation in the Federal District Court in Greensboro, North Carolina. The suit alleges that Brown & Williamson has violated the Federal Unfair Competition Law by simulating Liggett's QUALITY SEAL trademark design which is used to signify the quality of its generic cigarettes. The court papers assert that Brown & Wiliamson is seeking to capitalize on the goodwill associated with Liggett's QUALITY SEAL trademark which was designed and has been advertised and promoted as a guarantee to consumers that its generic cigarettes are of high quality. Liggett's promotional program for its QUALITY SEAL generic cigarettes includes the sponsorship of a Quality Seal Amphitheater at the New Orleans World's Fair. Liggett has asked the Court to enjoin Brown & Williamson from infringing Liggett's trademark and requests compensatory and punitive damages.

[Handwritten Note]
TO: DPC
FROM: EP

BROWN & WILLIAMSON TOBACCO CORPORATION

A member of the BATUS Group

1600 West Hill Street
P.O. Box 35090
Louisville, Kentucky 40232

GLENN M. GRATTA [Illegible] S. YOSEMITE
DEPARTMENT SALES MANAGER SUITE 203
ENGLEWOOD, CO 80112

July 10, 1984

D.P. CHRISTENSEN

Dear Don:

As I have mentioned to you several times in telephone conversations since our entry into the Generic cigarette segment, our customers have been literally deluged with negative comments and publications by Liggett & Meyers [sic] personnel, Gary Tobacco personnel and the General Products Corp. relative to our product, programs and activities. While some of these actions were both expected and one in the spirit of fair competition, much of it is in my opinion not only malicious and unfair, but also based on conjecture.

From the outset our intent has been to recapture the percentage of the business *we* have lost to Generic cigarettes. All of our sales activities and programs have been geared to that end. Our program and any modifications of it have been made available to *all* customers and the provisions have been consistently applied. Our program has been and remains competitive.

The following are examples of occurances [sic] of competitive activities that I feel to be unfair:

1) A mailgram from GPC to customers that alleged our Heartland products to be inferior and composed of low quality tobaccos. This mailgram further charged that our program was not being consistently applied and offered to all customers.

2) Numerous reports from my Division Managers that customers have been told by either GPC, Gary Tobacco or L&M personnel that we are trying to "put them out of business" or that we want to "take over the Generic segment" for the purpose of "killing it" or "stopping its growth".

3) Comments by a Mr. Al Cagney (either L&M or Gary Tobacco) to Karnett-Venger of Omaha, Nebraska that they (L&M) will match or exceed any and all B&W offers. Mr. Cagney, however, did not put anything in writing to support his comments.

4) Numerous reports to my Division Managers that customers were told by L&M personnel that we would be sued and prevented from shipping our product due to the fact that we had "copied" their packaging. These reports came to me over a period of several weeks *prior* to the initiation of *any* litigation against us.

5) A report from Division Manager, B. J. Redman – 23E that a Montana customer, F. T. Reynolds had been told by L&M that an *injunction* had been gained against us in North Carolina that would keep us from shipping orders. The customer was told that

"B&W won't be able to ship your order". The customer replied that he would maintain his agreement and order with B&W and wait and see for himself.

Don, it is one thing to compete on the basis of facts and obvious advantages that your product or program offer. It is an entirely different matter to attempt the same on the basis of conjecture and/or innuendo. Regardless, we continue to compete openly and fairly in the marketplace and represent our product and programs to the customer of our policies. For our part, we will continue to "take the high ground" of honesty and professionalism with our customers. If you have any comments, questions or require further amplifications please let me know.

As always, thanks for your help.

Sincerely,

/s/ Glenn -io.
Glenn M. Gratta

cc: L.W. Butler
H.E. Higgins
Sharon Smith

July 13, 1984

STATUS REPORT: Brown & Williamson Generic Entries

Sales

Brown & Williamson began shipments of its generic line-up on July 9, 1984. Our performance to-date has been encouraging:

– Through July 12, the Company has received initial orders exceeding 150 million sticks. This translates to about 2.8 million units for 1984.

– For 1985, accounts in hand alone should sell approximately 6.6 billion generic units, without any allowance for customers currently pending or private labels.

From an account standpoint, we have signed a number of larger distributors including Trade Development (projected 600 million generic units per year) and Bosart's (projected 375 million generic units per year). In regards to private labels, the Company is still in the process of intensive negotiations, and we expect final decisions with said accounts sometime in the next few weeks. In addition, the military has also begun taking orders for generic product.

* * *

Brown & Williamson continues to believe that the Company's generic program is both lawful and highly competitive. However, primarily to avoid public relations problems that might hinder us from selling and shipping orders for generic products, the Company has elected to aggressively move to have the case withdrawn or dismissed as early as possible. Accordingly, B&W is unilaterally taking steps to effect a number of changes in its package design, which will not hinder our marketing effort, but will answer Liggett's points of contention. It would then

be our intention to try to settle the case with Liggett out-of-court. The package changes include the following:

1. *B&W Closure Seal* – Brown and Williamson is moving to a closure design which includes the words "Superior Tobacco" and incorporates a lion graphic. The closure will continue to be printed in gold and black.

B&W Revised Closure Seal	Liggett Closure Seal

[Photocopy of cigarette package seals deleted in printing]

2. *B&W Leaf Design on Package* – Brown & Williamson plans to replace the leaf on this package with a generic design incorporating back-to-back letter B's capped by a crown.

B&W Revised "Branded" Package	Liggett "Quality Package

If B&W is unable to settle the case with the Liggett Group outside of court, we will ask the judge to terminate the case in some fashion. We plan to be in court if necessary within the next 10 – 14 days. One possible ruling might be that the judge would tell us not to use the leaf or the "Q", which we are already moving away from, and at the same time would rule that B&W's new product design is beyond any cavil.

If B&W is unsuccessful in having the case terminated, a normal course of action would see a number of months of discovery leading to a trial which could last up to a year or more.

The Law Department is confident that Liggett & Myers will not succeed in obtaining an injunction or any other court sanction which would constrain our current marketing effort.

* * *

Financials

B&W recently altered its generic offer to our customers. This change was again designed to keep B&W competitive. Brown & Williamson's current generic program pays in total from 55¢ per carton at the lowest volume level to 75¢ per carton at the highest volume level. This translates to a 79¢ per thousand trading profit, as shown in the following exhibit.

* * *

B&W

WEIGHTED AVERAGE COSTS/PROFITS

GENERIC BUSINESS

Per M Cigarettes

	Original Finan-cial	Round 2	Round 3	Round 4	1985
Trading Profit Pre Rebates	4.00	4.04	4.07	4.30	4.26
Less:					
Fixtures @ $.07/ carton (1)	.35	.35	.35	.35	.20
Volume Rebate (2)	1.30	1.68	1.54	2.22	2.22
Prompt Contract Rebate (3)	--	.47	.47	.47	A .24
Promotional Allowance (4)	--	--	.47	.47	.24
Sub-total	1.65	2.50	2.83	3.51	2.90
1984 TRADING PROFIT	2.35	1.54	1.24	.79	1.36

(1) To 6/30/85
(2) To 6/30/85
(3) To 6/30/85
(4) To 6/30/85

A – B&W composite offer $3.16.
L&M 7/9/84 offer assuming B&W mix $2.86.

July 10, 1984

[Illegible]
7/11/84

NEWSNEWSNEWS

LIGGETT & MYERS TOBACCO COMPANY, INC., Durham, N.C.

FOR IMMEDIATE RELEASE JULY 18, 1984
CONTACT: CAROL JOVA 919-683-8992

Liggett Group Inc. announced today that it has filed an amended complaint in Federal District Court in Durham, North Carolina against Brown & Williamson Tobacco Corporation seeking damages for alleged violations of the antitrust laws in the cigarette market and injunctive relief to bar such practices.

Liggett, the smallest major U. S. manufacturer, accounted for less than 5% of total domestic 1983 cigarette sales. More than half of Liggett's sales were in the generic segment of the cigarette market. B&W, the nation's third largest cigarette manufacturer, accounted for approximately 11% of domestic cigarette sales, all of which were of branded cigarettes where margins are substantially higher.

The amended complaint alleges that B&W, which has recently announced it is entering the generic segment, is engaged in unlawful predatory pricing designed to eliminate Liggett as a competitor in the marketplace.

FIELD SALES NOTICE **URGENT**

B&W

TO: ALL FIELD MANAGERS EXCEPT SPECIAL MARKETS

GENERICS/PRIVATE LABEL
PRODUCT INFORMATION

As promised in previous communication, we plan to remain competitive in the Generic/Private Label business. Consequently, we are pleased to announce two additional competitive revisions to our Generic/Private Label Offer.

1) New Volume Rebate Offer

Effective immediately, we have a new per carton offer as shown below.

QUARTERLY CASE VOLUME	PER CARTON ALLOWANCES REBATE	BONUS REBATE	PROMO ALLOWANCE	TOTAL
0-400	40¢	$.10	$.10	60¢
500-999	45¢	$.10	$.10	65¢
1000-1499	50¢	$.10	$.10	70¢
1500-7999	55¢	$.10	$.10	75¢
8000+	60¢	$.10	$.10	80¢

The above offer (including bonus rebate and promotional allowance) is good through June 30, 1985.

All customers from whom we've received orders/agreements will automatically receive this new rebate allowance.

#DS-2494
07/19/84

LIMITED

MEMORANDUM

TO: Mr. C. J. Heger
FROM: Mr. A. C. Diebold

DATE: July 26, 1984

SUBJECT: *Liggett Strategy In Regard To Generics*

I have made a very rough cut at this question as sufficient time was not available. My first step was to determine the estimated Variable Cost and Margin for Liggett's Generics and the associated Manufacturing Overheads. I used B&W's cost as a basis and adjusted them as follows:

A. *Leaf Cost* – B&W's current cost is estimated at $3.75 per M. I have always felt that Liggett probably has a cheaper Leaf Blend (possible increased usage of off-shore from their Brazilian subsidiary); therefore, I cut B&W's cost by 5%.

B. *Labor Cost* – B&W's Labor Cost based on Macon's manning is $.46 per M. This is probably considerably lower than Liggett's Durham Plant. However, to be conservative I increased this cost by only 10%.

C. *Other Variable Cost* – Casing, Wrapping, Filter, Freight and Excise Tax was assumed to be the same as B&W's.

The results of the above calculation produce a margin for Liggett's Generics before rebates, etc. of $4.77 per M. This compares to $4.65 per M for the B&W products.

In regard to overheads, our previous study (Liggett acquisition) indicated Durham's overheads amounted to $40.8 million for a volume of 39 billion. Since we are still

in the same volume range we used this same figure. On a full allocated basis this would work out to $1.09 per M. The $40.8 million estimated was based on an incremental overhead cost (incremental to established branded products of $.50 per M).

The volume assumptions are critical to anticipating Liggett's strategy. I discussed this with Hal Hughes who had the following thoughts:

> Mr. Hughes believes the Generic market is still growing and with B&W having entered the markets, and other potential entrants into the market (it is rumored that Lorillard is about to enter), Hal believes the market will continue to grow over the foreseeable future. He estimates a total Generic volume of around 30 billion for 1984, possibly more. Hal feels current B&W projections are a bit high and anticipates a B&W volume

* * *

As can be seen the operating income for Generics is only $9 million. This reduces the total operating income to around $42 million as opposed to the previous fiscal year of $51 million.

We are also showing on Schedule II the likely reduction in Interest Income which should result as the working capital requirement to sustain the incremental volume increases. The figure was based on variable cost including the duration factor for leaf and a 13% interest rate was computed. After taking this cost into account, the Generic volume is producing a pre-tax loss of $18 million.

Summary

Turning to the direct question asked i.e. – What will Liggett do and how long can they hold on? My thoughts are as follows:

First we already know that Grand Met is attempting to dispose of the tobacco business. The entry of B&W into the business has driven down the potential price for the business and has spoiled the financing for the leveraged buyout. While the Liggett Group is no doubt mad as hell, and may desire to do anything to stop B&W, from Grand Met's viewpoint they need to find a buyer and protect the potential selling price as much as possible. I would doubt that they would allow Liggett to continue to meet and beat our cigarette selling prices and will probably attempt to raise prices as soon as possible. In short I believe that they have or will shortly decide to share the market with B&W and others. In the meantime they will probably continue to search for a buyer. I fear that if B&W does not purchase Liggett, they could be sold to someone such as U. S. T. of Culbro.

As to Liggett's staying power, if B&W continues to cut prices, they will be forced in the short term to meet our prices, but not to beat them. They would count on B&W increasing price around the first of the year or sooner. If they can't find a buyer at any price, their long term strategy would be to milk the entire business.

If I can be of further help, please let me know.

A. C. D.

/af

[In Evidence August 17, 1984]

GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT I)

L&M (June 4, 1984)

(1)	(2)	(3)		(4)		(5)	(6)	
		BONUS/ DIS./ALLOW		REBATES				
CASES/ (QTR)	LIST (CTN)	GPC	FRAN	ADV.	CTN. PUR.	RETAIL PROMO.	NET COST GPC	NET COST FRAN
0-99	$3.75	$ 0	$ 0	$0	$0	$.077	$3.673	$3.673
100-199	3.75	0	0	.09	0	.077	3.583	$3.583
200-499	3.75	0	.10	.09	0	.077	3.583	3.483
500-999	3.75	0	.13	.09	0	.077	3.583	3.453
1,000-1,499	3.75	0	.13	.09	0	.077	3.583	3.453
1,500+	3.75	0	.13	.09	0	.077	3.583	3.453

B&W (June 4, 1984)

CASES/ (QTR)	LIST (CTN)	BONUS/ DIS./ALLOW	REBATES	RETAIL PROMO.	NET COST
0-99	$3.75	–	$ 0	–	$3.75
100-199	3.75	–	.10	–	3.65
200-499	3.75	–	.15	–	3.60
500-999	3.75	–	.20	–	3.55
1,000-1,499	3.75	–	.25	–	3.50
1,500+	3.75	–	.30	–	3.45

(1) Bracket structure by volume of cases sold per quarter.

(2) List price per carton.

(3) Bonus, discount and allowance monies. L&M column segmented for GPC (combination) and franchise. NOTE: B&W's column is not segmented.

(4) Rebate monies are segmented for L&M into advertising and carton purchase.

L&M (ADV.) – $.09 based on maximum rate of $.12 annualized. It is offered only 3 quarters/year. ($.75 x $.12 = $.09)

B&W – rebate schedule established for all customers based on volume.

(5) Retail promotion (L&M) – Because of the 14 state Doral areas, L&M responded with a 13-week dollar off retail price stickers. One week's purchases qualified for these stickers. ($1.00 – 13 weeks = $.077)

(6) Net cost reflects annualization of all discounts, allowances, bonuses, rebates and promotional offers at maximum rate *plus* 100% participation.

/tm/1570B/1

GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT II)

L&M (6/18 Eff. 8/1)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW GPC	FRAN	(4) REBATES ADV.	CTN. PUR.	(5) RETAIL PROMO.	(6) NET COST GPC	FRAN
0-99	$3.75	$.045	$.005	$ 0	$.10	$.077	$3.528	$3.568
100-499	3.75	.045	.105	.09	.15	.077	3.388	3.328
500-999	3.75	.040	.135	.09	.20	.077	3.338	3.248
1,000-1,499	3.75	.045	.135	.09	.25	.077	3.288	3.198
1,500+	3.75	.045	.135	.09	.30	.077	3.238	3.148

B&W (June 21, 1984)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW	(4) REBATES	(5) RETAIL PROMO.	(6) NET COST
0-99	$3.75	$.10	$.10	–	$3.55
100-199	3.75	.10	.20	–	3.45
200-499	3.75	.10	.25	–	3.40
500-999	3.75	.10	.30	–	3.35
1,000-1,499	3.75	.10	.35	–	3.30
1,500+	3.75	.10	.40	–	3.25

(1) Bracket structure by volume.

(2) Per carton list remains the same.

(3) L&M (GPC) – Weighted average which includes 5¢ special full flavor sell-in rebate plus 4¢ GPC allowance. ($.04 x 90% volume) + ($.09 x 10% volume) = .045.

L&M (FRAN) – Includes full flavor rebate (5¢) plus franchise allowance of 0-13¢. Weighted average based on full flavor rebate at 10% volume as in GPC calculation. (.18 allow + full flavor x 10%) + (.13 allow x 90%) = .135.

B&W – Introduced 10¢ bonus rebate.

(4) L&M (ADV.) – Maximum rate of 12¢ annualized (.75 x .12 = .09) remains the same.

L&M (CTN. PUR.) – Carton purchase rebates began.

B&W – Rebates increases 10¢.

L&M – 13-week dollar off promotion remains the same.

(6) Reflects annualization of all offers at maximum rate plus 100% participation.

/tm/1570B/2

GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT III)

L&M (Week of June 21)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW GPC	(3) BONUS/ DIS./ALLOW FRAN	(4) REBATES ADV.	(4) REBATES CTN. PUR.	(5) RETAIL PROMO.	(6) NET COST GPC	(6) NET COST FRAN
0-99	$3.75	$.055	$.005	$ 0	$.10	$.077	$3.518	$3.568
100-499	3.75	.055	.105	.09	.15	.077	3.378	3.328
500-999	3.75	.055	.135	.09	.20	.077	3.328	3.248
1,000-1,499	3.75	.055	.135	.09	.25	.077	3.278	3.198
1,500+	3.75	.055	.135	.09	.30	.077	3.228	3.148

B&W (Week of June 9)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW	(4) REBATES	(5) RETAIL PROMO.	(6) NET COST
0-99	$3.75	$.10	$.10	$.10	$3.45
100-199	3.75	.10	.20	.10	3.35
200-499	3.75	.10	.25	.10	3.30
500-999	3.75	.10	.30	.10	3.25
1,000-1,499	3.75	.10	.35	.10	3.20
1,500+	3.75	.10	.40	.10	3.15

(1) Bracket structure by volume.

(2) List price per carton.

(3) L&M (GPC) – Allowance increases from 4¢ to 5¢. ($.05 allow x 90%) + ($.10 allow + full flavor x 10%) = $.055

L&M (FRAN) – 0-13¢ allowance plus 5¢ full flavor weighted average remains the same.

B&W – 10¢ bonus rebate remains the same.

(4) L&M (ADV.) – No change; Annualized at maximum rate.

L&M (CTN. PUR.) – Same schedule as Exhibit II.

B&W – Same schedule as Exhibit II.

(5) L&M – 13-week dollar off stickers are the same.

B&W – Introduced 10¢ promotion reserve.

(6) Reflects annualization of all offers at maximum rate and 100% participation.

/tm/1570B/3

[In Evidence August 17, 1984]

GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT IV)

L&M (July 5)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW GPC	FRAN	(4) REBATES ADV.	CTN. PUR.	(5) RETAIL PROMO.	(6) NET COST GPC	FRAN
0-99	$3.75	$.127	$.005	$ 0	$.20	$.154	$3.269	$3.391
100-199	3.75	.127	.005	.09	.25	.154	3.129	3.251
200-499	3.75	.127	.105	.09	.25	.154	3.129	3.151
500-999	3.75	.127	.135	.09	.30	.154	3.079	3.071
1,000-1,499	3.75	.127	.135	.09	.35	.154	3.029	3.021
1,500+	3.75	.127	.135	.09	.40	.154	2.979	2.971

B&W (July 9)

0-499	$3.75	$.10	$.35	$.10	$3.20
500-999	3.75	.10	.40	.10	3.15
1,000-1,499	3.75	.10	.45	.10	3.10
1,500-7,999	3.75	.10	.50	.10	3.05
8,000+	3.75	.10	.55	.10	3.00

(1) B&W bracket structure changes.

(2) List price per carton.

(3) L&M (GPC) – Allowance increases from 5¢ to 12.2¢. Also includes 5¢ full flavor based on 10% of volume. (.172 x 10%) + (.122 x 90%) = .127.

L&M (FRAN) – Weighted average of 5¢ full flavor at 10% volume and 0-13¢ allowance.

B&W – 10¢ bonus rebate.

(4) L&M (ADV.) – 12¢ maximum rate annualized (3 quarters).

L&M (CTN. PUR.) – Carton purchase offer increases 10¢.

B&W – Rebate increase an additional 10¢ all are indication of the new bracket structure.

(5) L&M – Doral response areas 13-week dollar off sticker offers revised July 18. Two-weeks stock now qualified. (2 ÷ 13 = .154)

B&W – 10¢ promotion reserve.

(6) Reflects annualization of all offers at maximum rate and 100% participation.

/tm/1570B/4

GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT V)

L&M (July 17)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW GPC	FRAN	(4) REBATES ADV.	CTN. PUR.	(5) RETAIL PROMO.	(6) NET COST GPC	FRAN
0-499	$3.75	$.127	$.105	$0	$.35	$.154	$3.029	$3.051
500-999	3.75	.127	.135	.09	.40	.154	2.979	2.971
1,000-1,499	3.75	.127	.135	.09	.45	.154	2.929	2.921
1,500-7,999	3.75	.127	.135	.09	.50	.154	2.879	2.871
8,000+	3.75	.127	.135	.09	.55	.154	2.829	2.821

B&W (July 18)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW	(4) REBATES	(5) RETAIL PROMO.	(6) NET COST
0-499	$3.75	$.10	$.40	$.10	$3.15
500-999	3.75	.10	.45	.10	3.10
1,000-1,499	3.75	.10	.50	.10	3.05
1,500-7,999	3.75	.10	.55	.10	3.00
8,000+	3.75	.10	.60	.10	2.95

(1) L&M restructures brackets to that of B&W.

(2) List price per carton.

(3) L&M (GPC) – 12.2¢ allowance plus 5¢ full flavor sell-in weighted average.

L&M (FRAN) – 0-13¢ allowance plus 5¢ full flavor sell-in weighted average.

B&W – 10¢ bonus rebate.

(4) L&M (ADV.) – 12¢ maximum rate annualized (3 quarters).

L&M (CTN. PUR.) – Offer increases 10¢.

B&W – Bonus rebate increases an additional 5¢.

(5) L&M – Doral 14 state, 13-week dollar off stickers for 2-week purchase qualifiers.

B&W – Promotion reserve.

(6) Reflects annualization of all offers at maximum rate and 100% participation.

/tm/1570B/5

CURRENT
GENERIC CIGARETTE PRICING SUMMARY
(EXHIBIT VI)

L&M (August 16)

(1) CASES/ (QTR)	(2) LIST (CTN)	(3) BONUS/ DIS./ALLOW GPC	(3) BONUS/ DIS./ALLOW FRAN	(4) REBATES ADV.	(4) REBATES CTN. PUR.	(5) RETAIL PROMO.	(6) NET COST GPC	(6) NET COST FRAN
0-499	$3.75	$.127	$.105	$ 0	$.40	$.105	$3.118	$3.14
500-999	3.75	.127	.135	0	.45	.105	3.068	3.06
1,000-1,499	3.75	.127	.135	0	.50	.105	3.018	3.01
1,500-7,999	3.75	.127	.135	0	.55	.105	2.968	2.96
8,000+	3.75	.127	.135	0	.60	.105	2.918	2.91

B&W (August 16)

0-499	$3.75	$.10	$.40	$.177	$3.073
500-999	3.75	.10	.45	.177	3.023
1,000-1,499	3.75	.10	.50	.177	2.973
1,500-7,999	3.75	.10	.55	.177	2.923
8,000+	3.75	.10	.60	.177	2.873

(1) Bracket structure bases on cases sold per quarter.

(2) Carton list price.

(3) L&M (GPC) – 12.2¢ allowance plus 5¢ full flavor sell-in weighted average.

L&M (FRAN) – 0-13¢ allowance plus 5¢ full flavor sell-in weighted average.

B&W – 10¢ bonus rebate.

(4) L&M (ADV.) – No longer available.

L&M (CTN. PUR.) – Offer increases an additional 5¢.

B&W – Bonus rebate.

(5) L&M – Dollar off stickers (2-week duration) for a period of 19 weeks. (2 – 19 = .015)

B&W – Announced dollar off stickers for 1-week duration for a period of 13 weeks (1 – 13 = 0.77) *plus* 10¢ promotion reserve.

(6) Reflects annualization of all offers at maximum rate and 100% participation.

/tm/1570B/6

[1984]

NATIONAL MANAGEMENT CONFERENCE

GENERIC/PRIVATE LABEL PRESENTATION

SLIDE 1 (TITLE SLIDE)

THANK YOU DAVE. WHILE THE PAST SIX MONTHS HAVE BEEN FILLED WITH CHALLENGES AND OPPORTUNITIES FOR ALL OF US, ANOTHER CHALLENGE AND OPPORTUNITY HAS BEEN ADDED TO MY PERSONAL AGENDA, AND THAT IS THIS YEAR HAVING TO DIRECTLY FOLLOW DON FISH – THE MASTER OF THE SOUTHERN VOCABULARY AND PRESENTATIONS. DON, OLD PARTNER, YOU'RE A TOUGH ACT TO FOLLOW. BUT I AM HAPPY TO BE HERE AND TAKE THIS OPPORTUNITY TO SHARE OUR PROGRESS AND PLANS IN OUR GENERIC/PRIVATE LABEL AREA.

SLIDE 2

AS ALL OF YOU ARE AWARE, WE'VE BEEN VERY SUCCESSFUL IN OUR GENERIC/PRIVATE LABEL PROPOSITION. WITH THIS KIND OF SUCCESS, IN ANY KIND OF INDUSTRY, NORMALLY COMES THE CHALLENGE OF COMPETITION. AS YOU ARE AWARE, WE HAVE BEEN CHALLENGED IN 1984 AND FEEL THAT WE HAVE NOT ONLY MET THIS CHALLENGE BUT ALSO ARE PREPARED TO MEET IT IN 1985 AND BEYOND.

SLIDE 3

I WOULD LIKE TO SPEND SOME TIME THIS MORNING DISCUSSING THIS CHALLENGE AND HOW IT RELATES TO OUR EVER CHANGING ENVIRONMENT, HOW IT RELATED TO OUR '84 PROGRAMS AND HOW WE'RE PREPARED TO MEET THIS CHALLENGE IN 1985 AND BEYOND.

SLIDE 4

How and why did the challenge of success develop? 1981 through 1984 was a period of unprecedented growth for us in the generic/private label area. In 1982, we grew at the rate of 160% over 1981; 1983 at a rate of 170% and our plan going into 1984 was to grow at 64% again. This growth, again, was unprecedented in the cigarette industry. We also established something that was again very unique to our industry and that was a very high level of trade participation in a program. For the first time in our industry, we developed a very unique partnership with the trade. They actually had a sense of "ownership" of the generic/private label proposition and grew to totally support our program together with their efforts. Prior to this period, no one in this industry really believed that the trade could become such an integral part of a national program. Generic cigarettes have grown from a base of "0" to now being sold by more than 95% of the nation's supermarkets and 90% of its wholesalers. Another important element of our success was the extremely high consumer acceptance that we received. Today's consumer was ready for a quality product at a fair price. This was truly not only a reflection of economic conditions, but as Don mentioned earlier, a reflection of changing consumer values. There also had to be a lot of non-believers in our industry since up and through mid 1984 we were fortunate not to have any competition in a category that was growing so fast. Liggett was the category and as the category grew, it became more and more attractive for competition to come in as it did in 1984. The program that we established was one that was considered very sophisticated for the cigarette industry but very necessary in carrying a

non-traditional approach to a very traditional industry. This "ownership" or partnership with the trade that we talked about earlier was established through a program of brokers, franchise distributors and private label customers. We feel it's very important that the principles of our generic/private label program that we have established stay a major piece of the foundation of our business as we look to grow in the future.

SLIDE 5

We've spent a lot of time recently talking about our environment and how the environment continually has changed. The effects of this environmental change can be identified in four major areas in the generic/private label program. These are: competition, the trade, our consumer and our organization. Let's spend some time now talking about the change in these four elements.

SLIDE 6

Competition in our category was the major change that we've had to deal with in 1984. It's important that we all understand how we feel our competition positioned themselves coming in and where we feel they are positioning themselves for the future. R. J. Reynolds was the first major competitor to enter the generic arena with their Doral brand which was positioned as a branded product at a generic price. They felt that they could put new zest in a previously unsuccessful brand for them. It was introduced in four styles: Filter Lights, Filter Light 100's, Light Menthol King and Light Menthol 100's. R. J. Reynolds had done their homework. When they introduced it in May of

1984, THEY WENT INTO 14 STATES – 14 STATES THAT REPRESENTED 44% OF OUR GENERIC/PRIVATE LABEL BUSINESS. BASED ON THE GROWTH THAT THE CATEGORY CONTINUED TO HAVE DURING THIS PERIOD, THEY DECIDED TO EXPAND THE BRAND NATIONAL IN JULY OF THIS YEAR. THEIR STRATEGY WAS TO USE THEIR LARGE RESOURCES, THAT IS, THEIR CLOUT, MONEY AND PEOPLE TO ENTER THIS GROWING CATEGORY. THEY ENTERED THE CATEGORY WITH DIRECT ACCOUNT INCENTIVES OF UP TO 30¢ A CARTON, FREE DISPLAYS FOR THE TRADE, DISPLAY PAYMENTS FOR THE TRADE AND A NATIONAL ADVERTISING PROGRAM. ALL OF THESE ELEMENTS WERE TRADITIONAL BRANDED MARKETING APPROACHES TO A NEW NON-TRADITIONAL CATEGORY.

SLIDE 7

AS A COMPANY, WE VIEWED R. J. REYNOLDS' ENTRY INTO THE GENERIC CATEGORY A LITTLE DIFFERENTLY THAN WE HAD VIEWED COMPETITION IN THE PAST. WE WERE THE BIG GUYS ON THE BLOCK. WE WERE THE EXPERT IN THE CATEGORY AND, MOST IMPORTANTLY, FELT A NEW ENTRY INTO THIS CATEGORY COULD DRIVE THE TOTAL CATEGORY UP. WE ASSUMED AN OFFENSIVE POSTURE. THAT WAS, ONE OF DRIVING THE TOTAL CATEGORY UP. YES, DORAL COULD GET A PIECE OF THE CATEGORY, BUT WE WOULD ALSO GROW AS THE CATEGORY GREW. WE WENT INTO THE 14 STATE AREA THAT R. J. REYNOLDS HAD GONE INTO WITH A VERY AGGRESSIVE PROGRAM THAT INCLUDED DIRECT ACCOUNT VOLUME INCENTIVES, RETAIL INVENTORY BUILD ALLOWANCES, FREE MERCHANDISING FIXTURES, CONSUMER PROMOTION THAT INCLUDED DOLLAR OFF STICKERING, 2 PACKS FREE WITH A CARTON AND BUY 4 GET 1 FREE, AND WE INCREASED OUR COVERAGE. WE BROUGHT IN CREWS OF PEOPLE AT BOTH THE RETAIL AND HEADQUARTER LEVEL. A TEAM EFFORT BETWEEN LIGGETT & GARY SALES PERSONNEL IS WHAT WAS NEEDED FOR THIS, AND A TEAM EFFORT WE RECEIVED. THE EFFORTS OF THE

FINEST SALES ORGANIZATION IN THE INDUSTRY RESULTED NOT ONLY IN INCREASE IN BUSINESS IN THE 14 STATE AREA BUT OVERALL A 25% INCREASE NATIONALLY IN JUNE FOR US. ALSO, OVER 5900 PMD'S WERE PLACED BY OUR ORGANIZATION DURING MAY AND JUNE IN THE 14 STATE DORAL TEST AREA. BUT R. J. REYNOLDS IS A FORMIDABLE COMPETITOR, AND THEY ARE NOT GOING TO GO AWAY, AND EVEN THOUGH THEIR INITIAL MOVEMENT OR CONSUMER PULL WASN'T WHAT THEY PROBABLY EXPECTED, WE FEEL THAT THEY ARE GOING TO BE THERE AT RETAIL. THE DAY TO DAY, STORE TO STORE BATTLE FOR DISTRIBUTION AND MERCHANDISING SPACE IS GOING TO BE ONE THAT WILL BE WON AT RETAIL.

SLIDE 8

BROWN & WILLIAMSON WAS THE NEXT MAJOR COMPETITOR TO ENTER THE GENERIC CATEGORY. THEY FELT THAT THEY COULD USE THEIR CLOUT, MONEY AND PEOPLE, TO REALLY STRIKE AT THE HEART OF OUR BUSINESS AND THAT IS THE BLACK AND WHITE GENERIC PRICED PRODUCT. THEY FELT THEY COULD RIDE OUR COATTAILS OF SUCCESS BY INTRODUCING A PRODUCT AND A PROGRAM THAT HIGHLY RESEMBLED OURS. THEY CAME WITH ALL 8 STYLES IN JULY ON A NATIONAL BASIS. THE MAJOR DIFFERENCE IN THEIR PROGRAM WAS IS [SIC] THAT THEY OWN THEIR BRAND AND SELL IT TO THE ACCOUNTS VERSUS OUR PROGRAM WHERE WE CONTRACTED FOR THE BRAND TO CREATE ACCOUNT OWNERSHIP. THEIR PROGRAM WAS NOT ONLY VERY AGGRESSIVE BUT VERY EXPENSIVE TO THEM AND US. THEY OFFERED DIRECT ACCOUNT INCENTIVES THAT EVENTUALLY ESCALATED UP TO 80¢ A CARTON, FREE DISPLAYS, RETAIL INCENTIVES AND CONSUMER PROMOTIONS.

SLIDE 9

OUR POSTURE WITH BROWN & WILLIAMSON WAS DIFFERENT THAN IT WAS WITH R. J. REYNOLDS. WE FELT WE REALLY HAD TO TAKE A

defensive posture. Similarity of packaging and the difference in taste of the Brown & Williamson product to our product we felt could really hurt the generic category, and that is both for the consumer and the retailer. Our plan was to protect both the category and the base of business we had established. The management of our company, all the way through GrandMet, provided us with the resources and the commitment to protect this important base of business for us. We entered the pricing war, even though there was averagely [sic] an 8¢ difference in our incentive program and Brown & Williamson's, we felt that our credibility could make up this difference. We also filed a law suit against Brown & Williamson in the Federal courts for trademark infringement, wrongful package imitation and predatory pricing. Our retail program included both free displays and the array of consumer volume promotions that we had used in the Doral program. Again, a team effort is what was needed, and a team effort is what we received at both retail and headquarter coverage by both the Gary and Liggett field organizations. The results of this team effort were that we maintained 80-85% of the total category volume during the introductory period. But again, the battle shifted to retail. We are not only fighting distribution and merchandising at retail this time but also the awareness of our generic product versus that of Brown & Williamson with both the retailer and the consumer.

SLIDE 10

While the battle on a day to day or week to week basis is hot and heavy, it's important that we sometimes sit back and look and see how the entire war is fairing [sic]. At the

end of the first fiscal quarter of 1984, Liggett & Myers' generic and private label products represented over 3½% of the business for the quarter and were the entire category. Not only have we grown to almost a 4 share of market for the fourth quarter, but also as we had hoped, the entire category has grown to over a 5 share of the total cigarette business. Also, our fiscal YTD share of market exceeded 4%. As you can see from the total industry volume figures at the top of the chart, that in an industry that is flat, to show growth is an exciting accomplishment. We have not only maintained 80% of a growing category but have also sent a message out to the rest of the industry that Liggett & Myers cannot be walked on. This message is a result of the accomplishments of everyone in our organization and a special tribute to our Liggett & Gary field sales organization.

SLIDE 11

As Don mentioned earlier, today's consumer is changing, and we are seeing this change in the generic/private label consumer. The Private Label Manufacturer's Association 1984 Gallup Poll research indicates that: #1 – 80% of consumers consider quality very important in the decision to buy a store brand and 74% price. This says that quality is as important in the consumer's mind as lower prices. Second, 36% of the consumers say they are buying more store brands this year and 42% expect to purchase more next year. More people today than ever before are willing to lay a store brand or generic brand on the table and say this is the brand that they smoke. And third, it is very interesting that 53% of the consumers would be influenced

TO BUY STORE BRANDS IF THERE WAS A GUARANTEE OF SATISFACTION. THIS IS AN IMPORTANT ELEMENT THAT WE PLAN TO ADDRESS IN 1985. YANKELOVICH HAS ALSO TOLD US THAT WHILE THE PROLIFERATION OF GENERIC/PRIVATE LABEL BRANDS HAS INCREASED THE CONSUMER'S ALTERNATIVES, IT HAS DECREASED THE CONSUMER'S PERCEPTION OF QUALITY CONTINUITY. MR. OR MRS. CONSUMER IS CONCERNED THAT EACH TIME THEY MAKE A DECISION TO BUY A STORE BRAND OR A GENERIC BRAND THAT THE SAME QUALITY IS CONSISTENTLY THERE. WE FEEL THAT THE CONSISTENCY OF THE QUALITY OF LIGGETT & MYERS' STORE BRAND PRODUCTS IS SOMETHING THAT HAS TO CONTINUALLY BE DRIVEN HOME TO THE CONSUMER IN THE FUTURE.

SLIDE 12

COMPETITION AND THE CHANGING VALUES OF THE CONSUMER HAS ALSO CAUSED A CHANGE FOR THE TRADE. FIRST, COMPETITION IN THE GENERIC CATEGORY HAS NOW GIVEN THE TRADE A CHOICE. THEY NO LONGER HAVE TO WAIT FOR US, AND THEY HAVE THE OPPORTUNITY TO LEVERAGE COMPANY AGAINST COMPANY. WE HAVE TO BE THERE FIRST AND ON A CONSISTENT BASIS. SECOND, THE GROWTH OF THE GENERIC CATEGORY HAS INCREASED THE RETAIL INFLUENCE OF DIRECT ACCOUNT DISTRIBUTION. THE SHEER NUMBERS OF THE CONSUMERS IN THE GENERIC AND PRIVATE LABEL CATEGORY HAVE CREATED A VOICE, OR A MESSAGE, TO THE RETAIL ACCOUNT. THIS VOICE CAN MORE, NOW THAN EVER, INFLUENCE WHAT THE DIRECT ACCOUNTS WILL CARRY. THIRD, THERE HAS ALSO BEEN A TREND IN THE INDUSTRY TOWARDS UPGRADED GENERIC/PRIVATE LABEL PACKAGING. KENTON GAST, VICE PRESIDENT OF PROCUREMENT OF THE KROGER COMPANY, STATED THAT THE CONSUMER MUST SEE OUR PRIVATE LABEL PRODUCT AND ASSOCIATE IT WITH HIGH VALUE AND QUALITY. WHILE BLACK AND WHITE IS NOT DEAD, MORE CONSUMERS THAN EVER BEFORE ARE CONSIDERING

STORE BRAND PRODUCTS OR UPSCALE PACKAGING PRODUCTS TO BE THAT OF COMPARABLE VALUE AND QUALITY OF NATIONAL BRANDS.

SLIDE 13

THE CHANGE IN THE ENVIRONMENT HAS ALSO TOLD US THAT WE HAVE TO WORK DIFFERENTLY AS AN ORGANIZATION. THE CHANGING NATURE OF THE CATEGORY AND COMPETITION HAS INCREASED THE INTERDEPENDENCIES BETWEEN THE GARY ORGANIZATION AND THE LIGGETT ORGANIZATION AND THAT'S BOTH AT THE FIELD SALES LEVEL AND THE HEADQUARTER LEVEL. YES, BOTH SPECIALISTS AT THE RETAIL LEVEL AND THE HEADQUARTER LEVEL ARE IMPORTANT, BUT THE COMMUNICATION AND INFORMATION LINK BETWEEN THE TWO IS MORE IMPORTANT THAN IT EVER WAS BEFORE.

COMPETITION IS HERE TO STAY. WE HAVE TO DIRECT OUR RESOURCES TO WHAT WE CAN CONTROL. WE CANNOT CONTROL COMPETITION, BUT WE CAN CONTROL OUR PACKAGING, OUR PRICING, AND THE TASTE AND QUALITY OF OUR PRODUCT. OUR MIND'S SET, AS AN ORGANIZATION, HAS TO BE OFFENSIVE VERSUS DEFENSIVE – REALLY GEARED OR ZEROED INTO THOSE AREAS THAT WE CAN CONTROL. ALSO, OUR CHANGING ENVIRONMENT WILL INCREASE THE NEED FOR MANAGERS WHO UNDERSTAND THE ENVIRONMENT AND DECENTRALIZED DECISION MAKING FOR BOTH TIMELY ACTIONS AND REACTIONS.

SLIDE 14

WE HAVE WORKED HARD TO ENSURE THAT IN OUR GENERIC/PRIVATE LABEL ORGANIZATION WE ARE ORGANIZED TO MEET THE CHALLENGE OF CHANGE AND SUCCESS. OUR HEADQUARTERS STAFF IS COMPOSED OF DIDI HUNT, WHO HANDLES OUR MARKETING OPERATIONS; MIKE OSBORNE, IN CHARGE OF NATIONAL SALES; AND

4 national account managers who handle the corporate headquarter calls, including Steve Kirchhoff in the broker area; Joe McGee the distributor area; Charlie Harrison, the supermarket area; and Bruce Parsons in the convenience and drug area. This team not only develops our generic/private label programs but also jointly make [sic] those decisions necessary to carry on the day to day operations of our business and move us forward. Also, while we may develop a program in headquarters, the decisions on how that program is executed and implemented are made by those people who are closest to the action and that is both the Gary field sales organization and the Liggett field sales organization. While each piece of the organization has its own responsibilities and accountabilities, the tie and link between the two are now more important than it ever was before. I would like to stop here for just a second and commend and recognize this fine group of people. During my transition period into my new position, when I couldn't find my way to the bathroom, these are the people that made it happen in headquarters. And while we have always known that these players are good, it helped provide me with a sense of confidence that we can make it happen.

SLIDE 15

While our environment was changing rapidly in 1984, we implemented and executed some exciting marketing programs that we feel are helpful for us to build a base for the future.

SLIDE 16

At the beginning of 1984, we announced our Quality Seal program. Our marketing objective was to maintain the Gary Tobacco Company leadership position among consumers. Our strategy was to establish Gary Tobacco Company generic/private label cigarettes as the quality generic brands. Our creative objective was to convince users of generic/private label cigarettes that Gary Tobacco Company cigarettes are those of quality.

SLIDE 17

To announce the Quality Seal, we ran a national program that included several elements. First of all, we ran a national advertising program with full and half page newspaper ads in all major markets during November, December and January. This ad visually put the Quality Seal in front of the consumer.

SLIDE 18

Based on the previous experience we had with our excise tax program in 1983, we learned that we could get the retailer to participate in a national advertising program. Not only did we have over 500 participants in our cooperative advertising program, but most major retail organizations in the country participated.

SLIDE 19

A complete line of point of sale was developed to announce this program at the retail level. This included

INSERTS FOR OUR PERMANENT MASS DISPLAYS, PERMANENT COUNTER DISPLAYS, AS WELL AS TEMPORARY POINT OF SALE. During this period, over 6800 additional PMD's were placed and 8300 PCD's were place.

SLIDE 20

Our advertising program was also supplemented by a full blown public relations effort. This included a press conference and press releases to major publications across the country which stimulated both trade and consumer publications to run articles touting the Quality Seal and the growth of the generic/private label cigarette category.

SLIDE 21

Our public relations effort also included a full blown effort in broadcast media. CBS radio did an interview with K. v. Dey. It was carried on both AM stations and FM stations across the country. The news-sports radio network aired a news brief that ran over 1200 times and reached a 17.3 million nationwide audience. The North American press syndicate ran a news brief that 229 stations carried to over a 13 million audience and a TV video quip was developed that aired on 15 stations reaching over a 2 1/2 million audience. If I can now, I would like to take just a moment to play the CBS interview with K. v. Dey.

SLIDE 22

Our second major thrust against the Quality Seal was a sponsorship in the 1984 Louisiana World's Fair. Our objective was again to increase the consumer awareness of

Liggett & Myers' Quality Seal generic cigarettes. Our strategy was to use a major event, such as the Louisiana World's Fair, as a stimulus, or we might call it a swizzle stick, to increase the trade participation and ownership in the Quality Seal. When a retailer carried Quality Seal generics or store brand cigarettes, he was in essence carrying the official cigarette of the 1984 Louisiana World's Fair. Our involvement included sponsorship of the International Amphitheatre, which would host top name entertainment throughout the duration of the fair; a cooperative advertising program, which tied retailers into the World's Fair; mass sampling at the fair; theme related point of sale for retail, and again a full blown public relations campaign.

SLIDE 23

As you can see, the Amphitheatre was a massive structure built for the World's Fair that carried plenty of recognition for Liggett & Myers and the Quality Seal.

SLIDE 24

The stage of the Amphitheatre also carried this same recognition for Liggett & Myers and the Quality Seal. No matter where a picture was taken inside the Amphitheatre, recognition and exposure of the Quality Seal was always there.

SLIDE 25

As you flew into New Orleans and passed over the World's Fair, the Quality Seal was also visible on the top

of the Amphitheatre. I can also guarantee you that while we have a tough organization, there was no one in our organization that was tough enough to go on the top of the Amphitheatre and paint the Quality Seal up there.

SLIDE 27

Bert Parks, of Miss America fame, was chosen as the official spokesperson and announcer for the Liggett & Myers Quality Seal Amphitheatre. Bert was an admirable host to the top name entertainment that came in to perform at the World's Fair. Bert received high marks, not only being a great host, but also a fun person to work with. An interesting point is also that during the entire period in which major entertainment appeared in the Amphitheatre, it was *sold out*!

SLIDE 28

Our cooperative advertising effort with the retailers again proved to be very successful. The Louisiana World's Fair and our sponsorship with the Amphitheatre stimulated what was needed to get retailers to give their total support to the program. Again, we had over 500 participants in our cooperative advertising effort.

SLIDE 29

A special pack of Quality Seal generic cigarettes was developed as the official cigarette of the World's Fair and over 700,000 sample packs were passed out during the duration of the fair.

SLIDE 30

A complete line of theme point of sale showing the World's Fair logo along with the Quality Seal was developed for all of our placements at retail.

SLIDE 31

Our public relations effort included a press kit that was sent to national and local publications. The story of the World's Fair, Bert Parks and Liggett & Myers' involvement went across the country.

SLIDE 32

Our public relations effort also again included broadcast media. Events such as the sponsorship announcement, the Bert Parks hosting announcement, Bert Parks' interview and tour across the country, including the KABC-TV Hour Magazine, and a July 4th special at the Amphitheatre all provided events that were newsworthy for live media. The results were that we had over 1500 radio spots at a 60 second average where Liggett & Myers and/or the Quality Seal were mentioned – over 40 TV spots – reaching a combined audience of over 20 million viewers and listeners. I would now like to show you a video tape that summarizes our success at the 1984 Louisiana World's Fair.

(Play video tape.)

While the World's Fair itself may have had mixed reviews, we give it high marks in helping us carry our Q-Seal message.

SLIDE 33

In June, we also extended our product line to include both Full Flavor King Size and Full Flavor 100's, and as you can see from this chart, after initial pipeline figures in June and July, Full Flavor sales have continually grown to over 14,000 cases in sales in the month of October.

SLIDE 34

1984 was a busy, exciting year for all of us, but the proof is always in results. Our objective of 23 billion units was exceeded by shipping 23.9 billion units for the fiscal year. Our objective of a 3.6 share of market was exceeded by growing to over a 4% share of market for fiscal 1984. These positive results and growth provide us with a base to move ahead in 1985.

SLIDE 35

What are the issues for 1985 as we move forward in the generic/private label program? First of all the total category – will it grow? We feel confident it will. Will current or new competition increase this growth? What will be the impact of new pricing tiers on the growth of the generic/private label category. We feel that both activity by the industry and the changing values of the consumer will cause this category to continually grow. Second, Liggett & Myers generic/private label/consumer awareness – a key issue for 1985 – but we do have a difference – the Quality Seal and we plan to drive Quality Seal forward in 1985. Third, in protecting our current user base and Liggett generic/private label availability,

retail merchandising and direct account availability are both key elements. We have to be prepared for the battle for both distribution and merchandising space on our products in 1985.

SLIDE 36

We are investing a tremendous amount of resources in our generic/private label proposition in 1985 because we feel confident that the category will continue to grow. In 1983, the category showed 178% increase over the previous year. in 1984, a 82% increase. If the category continues to grow just at the same rate, it can be close to 50 billion units by 1988. People outside our company also feel it will grow. John Maxwell, industry analyst, says it will be 10-12% share of market by 1985, Samuel Bernstein of Bernstein Research, a financial analyst, said 5$^1/_2$-6% by 1984 [sic] and 10-12% by 1988. Even R.J. Reynolds, one of our major competitors, has stated that the generic category will represent 7-10% of the total cigarette market. Yes, we do feel the generic category will grow and we can grow with it.

SLIDE 37

Our objective for 1985 is to maintain the major share of the generic/private label category with programs that combat competitive entries and build our consumer franchise. Our volume objective is 26 billion units, which represents an 8.7% increase over our 1984 results. Now let's take some time to talk about each of our strategies.

SLIDE 38

Even though our direct account program is costly, it's a necessary evil in order to maintain distribution at the important direct account level. We are prepared to employ our tactics to combat entries at the direct account level including contract incentives, a contract bonus, our direct account volume incentives as we need in 1985 to fight the competititive onslaught. Another important element of our direct account program is to ensure that our coverage of direct accounts is frequent enough to not only meet the needs of the changing environment but to also meet those needs caused by competition. Liggett's sales organization has and will play a vital role in helping us ensure that we get the proper coverage on our headquarter accounts.

SLIDE 39

In October, we kicked off our Fall Consumer Retailer Volume Promotion which we are currently involved with. This program includes dollar off stickering, 2 packs free with a carton, and buy 4 packs get 1 free. The selling brochure, as well a full line of point of sale, were developed for this program and are currently being placed at retail. While this kind of a program doesn't stress for new trial and awareness, it is a good defensive strategy to help us with retailers and consumers during this competitive battle.

SLIDE 40

Driving home awareness of our Quality Seal is more important in 1985 than it ever has been before. Even though all

black and whites may look the same, the Quality Seal can give the retailer and the consumer the assurance that Quality Seal represents the original and accepted quality generic cigarette. In '85, we are moving ahead with putting the Quality Seal on our cartons, developing a Quality Seal slogan, developing the Quality Seal consumer guarantee, and a spring promotion to further enhance our awareness of Quality Seal.

SLIDE 41

The similarity between Brown and Williamson's carton packaging and our carton packaging has increased the need to bring a point of difference into our packaging, and that difference is putting the Quality Seal on the carton. We have already received approval from accounts that represent over 72% of our business to put Quality Seal on their cartons, and this includes the brands that we own, Class 'A' and franchise, and also our broker brands. Some of our top private label customers in the country have also given us approval to move ahead and put Quality Seal on the carton. All of our customers who have labels produced by us will be contacted and sold this concept. I'm sure you are all also aware that we maintain inventories of cartons in Durham, and we are working as hard as we can to get Quality Seal on the current inventories we have and develop new cartons as we deplete these for all of the brands we produce. Our goal is to have Quality Seal on all of the cartons at retail by January 1985.

SLIDE 42

While we've done a good job in 1984 of developing and promoting the Quality Seal, we did learn that our Quality

Seal awareness was not as high as we would like it to be. There is a need to develop a straight-forward, hard-hitting slogan that really communicated the message of the Quality Seal – something that the consumer would remember. The slogan, "There is no substitute for quality," was developed to be used on all future advertising and promotions. We hope this slogan can become another "Coke Is It" for the generic/private label cigarette industry.

SLIDE 43

As we discussed earlier, today's generic/private label consumer is more concerned than ever over the quality of generic/private label products. They've also expressed that a guarantee of satisfaction, or quality, could influence their purchase of generic/private label products. Our Quality Seal consumer guarantee, we feel, helps answer those needs as well as another step toward increasing the awareness of the Quality Seal. We want to ensure the consumer that the Quality Seal generic cigarettes are of the finest quality. The elements of this program are a pack back guarantee to the consumer, if for any reason, they are dissatisfied with the quality of Quality Seal generic or store brand cigarettes. We will back this with national advertising November through February. Based on our previous success with retailer advertising, we will again give our retailers the opportunity to participate in this program. We will also have a hard-hitting trade advertising program as well as a full blown public relations campaign and point of sale that touts the Quality Seal consumer guarantee. Our Quality Guarantee is a first for our industry and one of the few product guarantees in the

entire generic/private label category. We feel that this is another example of our leadership and innovation.

SLIDE 44

Our national advertising program will run through February in *USA Today* and *National Enquirer* with over 100 million impressions, "Quality Guaranteed – Look For The 'Q' And Be Sure." We feel confident that both the copy and the graphic treatment of the Quality Seal in this ad will help us get our message across that Quality Seal generic cigarettes are the quality choice.

SLIDE 45

Retailer ads have been developed for this program to give retailers the opportunity to participate in the quality guarantee program. A supply of these ads has been sent both to field personnel and are available in additional quantities here in Durham.

SLIDE 46

Letting the trade know that there is a difference is a very important element of our Quality Seal guarantee program. This ad with K. v. announcing our quality guarantee program to the trade will be run in all major trade publications throughout the duration of the program. Who can think of a better person to say, "Our quality guarantee stands for sales and profits with a capitol Q." We feel that both K. v.'s credibility with the trade and his message will have impact in our trade advertising.

SLIDE 47

We will support our Quality Seal guarantee with a full blown public relations effort. The campaign includes a news conference held in Durham to announce the quality guarantee to the media with a press kit that went out to all major and local publications in the country. Additionally, a consultant or spokesperson is being selected to serve as a consumer reporter for Liggett & Myers. This consultant will be a quality expert to address the consumer on a national tour with groups of consumers who are concerned about quality. We feel this will also give play in the dollar-wise sections of newspapers.

SLIDE 48

Our consumer guarantee program also includes a full array of both selling materials and point of sale to get the Quality Seal message and consumer guarantee across at the point of purchase. We feel we have an important story or message to tell the retailer and the consumer, and these selling and point of sale materials will help us do that.

SLIDE 49

We are not going to stop here on Quality Seal. We feel that we have a consistent message that we can tell. We are currently developing a program for the spring that will again drive home the Quality Seal message to the consumer. We want a consumer promotion that creates some trial but strong awareness of the Quality Seal. We hope to start this program in March and run it through

June. We think it's important that this program reinforces the awareness of Quality Seal, reinforces the smart shopper concept and can physically involve the consumer with the Quality Seal in some format.

SLIDE 50

We have also learned that increasing the number of styles we have available on our generic/private label products can help us to increase our business. Our current styles represent and appeal to approximately 72% of the total cigarette consumption. We feel that increasing style availability can capitalize to a broader base of consumers, and Full Flavor Menthol currently offers the best opportunity for us for expansion. First of all, the size of the market is significant, and we also think that it is a good competitive move to catch our competition with a Full Flavor Menthol while their efforts are being put in other areas.

SLIDE 51

As you can see from this cart, the total menthol category, while it has not grown, has remained comparatively stable over the past few years. Full flavor menthol represents 48.6% of the menthol category or almost half the total menthol sales, and this represents 13.4% of the total industry volume. We think that's a significant chunk of volume that we can go after.

SLIDE 52

In looking at 1984 top 10 full flavor menthol brands, you can see that the top 10 brands represent 97% of the total

FULL FLAVOR MENTHOL VOLUME. WE ALSO FEEL THAT, BASED ON THE SUCCESS OF NEWPORT, BOTH KOOL AND SALEM ARE VULNERABLE AND THAT WE CAN GET A SIGNIFICANT PIECE OF BUSINESS FROM THESE BRANDS. THE AVERAGE TAR LEVEL OF THESE TOP BRANDS IS IN THE 16 TO 17 MG. OF TAR LEVEL, AND THE TIPPING SKEWS TOWARDS CORK TIPPING ON THE KING SIZE AND WHITE TIPPING ON THE 100'S.

SLIDE 53

WE ARE READY TO ROLL ON OUR FULL FLAVOR MENTHOL. THE PRODUCT IS 16 MG. OF TAR WITH CORK TIPPING ON OUR KING SIZE AND WHITE TIPPING ON THE 100'S. WE PLAN TO HAVE CLASS 'A' READY TO SHIP IN MID-DECEMBER, OUR BROKER AND FRANCHISE BRANDS READY TO SHIP IN JANUARY AND BEGINNING IN FEBRUARY, IN SELLING AND SHIPPING OUR PRIVATE LABELS OUT. YOU WILL BE RECEIVING SHORTLY A FULL LINE OF BOTH SELLING MATERIALS AND POINT OF SALE TO SUPPLEMENT THIS ENTRY.

SLIDE 54

THE FIGHT FOR SPACE IN 1985 TO KEEP OUR PRODUCT AVAILABLE TO THE CONSUMER WILL BE HOT. WE FEEL THAT IT'S VERY IMPORTANT THAT WE REMAIN FLEXIBLE AND AGGRESSIVE IN DEVELOPMENT OF OUR MERCHANDISING CONCEPTS. WE FIRST OF ALL WANT TO ENSURE THAT WE PROPERLY UTILIZE AND MANAGE THE CURRENT FIXTURES WE HAVE AT RETAIL AND THAT INCLUDES OVER 67,000 PMD'S AND 83,000 PCD'S. THIS INCLUDES TIMELY P.O.S. FOR THESE RACKS AS WELL AS FAST TURNAROUND ON ORDERS. WE'RE PREPARED TO MEET COMPETITION WITH OUR FREE RACK PROGRAM, AND WE'RE PREPARED TO EXTEND THAT PROGRAM AS WE NEED. ADDITIONALLY, WE'RE PREPARED TO ORDER ADDITIONAL RACKS AS NEEDED DURING 1985 TO BE SURE WE'RE THERE AT RETAIL FOR THE

CONSUMER. ALSO, THE ONSLAUGHT OF NEW RACKS FROM R. J. REYNOLDS, FROM BROWN & WILLIAMSON, AND FROM OUR OWN STRIDE PROPOSITION IS CREATING PRESSURE ON THE RETAILER TO MAKE A DECISION WHERE HE IS GOING TO HOUSE THESE NEW ENTRIES. IT IS VERY IMPORTANT THAT WE CONTINUE TO DEVELOP NEW CARTON AND PACKAGE FIXTURES TO ENSURE AVAILABILITY AND COMBAT COMPETITION AND ALSO MEET THE NEEDS OF THE RETAILER. THE FIRST STEP WE'VE TAKEN IN THIS DIRECTION IS TO DEVELOP WHAT WE CALL A UNIVERSAL CARTON FIXTURE. WE'VE DEVELOPED 100 OF THESE RACKS WHICH ARE BEING TESTED OCTOBER THROUGH DECEMBER, AND WE ARE PREPARED TO EXPAND THESE NATIONALLY IF THE CONCEPT PROVES SUCCESSFUL.

SLIDE 55

THE 2 PROTOTYPES OF THIS UNIVERSAL RACK SHOWN HERE IN THIS PICTURE HOLD FROM 165 CARTONS TO 700 CARTONS. WE FEEL THAT THIS RACK CAN BECOME THE ALTERNATIVE CIGARETTE PRICING CENTER FOR THE RETAILER WHO HAS THE SPACE DEMANDS CREATED BY PRICE SEGMENTATION AND NEW BRANDS. THE EFFORTS AND THE FEEDBACK FROM THOSE OF YOU INVOLVED IN THIS TEST IS VERY IMPORTANT TO ENSURING THAT THIS CONCEPT IS ON TARGET.

SLIDE 56

AS YOU CAN SEE, WE HAVE AN AGGRESSIVE ATTACK PLANNED FOR 1985 IN THE GENERIC/PRIVATE LABEL AREA. WHILE IT WILL BE A BUSY YEAR FOR ALL OF US, IT IS IMPORTANT TO HAVE THE ENTIRE YEAR COVERED TO ENSURE THAT WE MEET THE CHALLENGE OF SUCCESS.

SLIDE 57

THE CHALLENGE OF SUCCESS FOR GENERIC/PRIVATE LABEL GOES BEYOND 1985. FOR THE FUTURE, WE THINK THERE'S SOME OTHER AREAS THAT ARE IMPORTANT THAT WE ADDRESS. FIRST OF ALL, WE WANT TO LOOK AT DEVELOPING AN UPSCALE COMMON PRIVATE LABEL AND REALLY WHAT WE'RE SAYING IS THAT IF THERE'S A TREND TOWARD UPSCALE PACKAGING IN THE INDUSTRY, WE WANT TO BE THERE FIRST. WE ALSO FEEL THAT IF WE SEGMENT THIS GENERIC BUSINESS, IT WILL BE TOUGHER AND TOUGHER FOR COMPETITION TO COME INTO IT. WE'LL ALSO CONTINUE TO LOOK AT STYLE AVAILABILITY. NON-FILTERS, WHICH ARE CURRENTLY IN MILITARY AND TEST WITH ASHLAND PETROLEUM COMPANY, WILL BE CONTINUALLY MONITORED TO SEE IF WE CAN ROLL ON A REGIONAL BASIS; ULTRA MENTHOL, WHICH IS BEING TESTED AND SOLD IN THE MILITARY CLASS OF TRADE – WE WILL CONTINUALLY LOOK AT THAT; AND THE BOX CATEGORY, WHICH REPRESENTS OVER 14% OF THE TOTAL INDUSTRY VOLUME, REPRESENTS A CATEGORY THAT WE WILL CONTINUE TO EXPLORE. ADDITIONALLY, WE'RE NOT GOING TO BACK OFF OF OUR QUALITY SEAL PROGRAM. WE THINK QUALITY SEAL IS OUR POINT OF DIFFERENCE AND A WAY THAT WE CAN DRIVE HOME THAT WE HAVE THE ORIGINAL AND ACCEPTED GENERIC/PRIVATE LABEL PRODUCT TO THE CONSUMER.

SLIDE 58

YES, WE FEEL CONFIDENT THE GENERIC/PRIVATE LABEL CATEGORY WILL CONTINUE TO GROW AND THAT LIGGETT & MYERS GENERIC/PRIVATE LABEL PROPOSITION CAN GROW WITH IT. WE FEEL THAT WE HAVE THE FLEXIBILITY AND THE CREATIVITY TO REALLY SEGMENT THIS GENERIC/PRIVATE LABEL CATEGORY AND GROW WITH IT AS IT

GROWS. AND MOST IMPORTANTLY, WE THINK THAT WE CAN CONTROL OUR DESTINY. WE HAVE THE WHEREWITHAL TO GROW AND, MOST IMPORTANTLY, TO GROW PROFITABLY. THANK YOU.

FISCAL 1988 CATEGORY SALES PROJECTIONS

CATEGORY AND L&M

(BILLIONS OF UNITS)

ANNUALIZED GROWTH THROUGH 1988	1988 CATEGORY VOLUME	1988 CATEGORY S.O.M.*	1988 L&M VOLUME		
			85%	75%	65%
19.4%	46.2	8%	39.3	34.7	30.0
41.7%	69.4	12%	59.0	52.1	45.1
58.4%	86.7	15%	73.7	65.0	56.4

* BASED ON TOTAL INDUSTRY SALES OF 578 BILLION UNITS FISCAL 1988

1985 OPERATIONAL PLANS

DOMESTIC MARKETING

Table of Contents

* * *

Spending Principles

To spend competitively to achieve the 8.6 billion sticks.

Plans are to continue the following rebates in the domestic market for the first half of 1985:

- Volume rebate
- Prompt contract rebate
- Promotional allowance
- Fixtures
- Special promotion/contingency fund

On July 1, 1985, only the volume rebate and special promotion/contingency fund are scheduled to continue. Specific uses for promotion monies are still under discussion.

1985 Preliminary Generic Financials
(per M basis)

Net Selling Price	$18.86
Total Variable Cost	14.38
Variable Margin	$4.48
Rebates:	
Volume	$2.42
Prompt Contract	.24
Promotion	.24
Fixtures	.20
Special Promotion/Contingency	1.00
	$4.10
Overhead	$.38
Trading Profit	–

In the Military, the current offer, $3.15 for kings and $3.35 for 100's, is a straight fixed price.

Continue to spend by customer according to volume. The following table details how different volume classifications compare in terms of rebates.

[LOGO]
STRIDE

FEBRUARY 20, 1985

STRIDE SALES HAVE COME FROM FULL-PRICE BRANDS

- STRIDE GREW FROM THE JULY INTRODUCTION TO .5 SHARE OF TOTAL CIGARETTE SALES IN DECEMBER.

- DORAL, A DIRECT PRICE COMPETITOR TO GENERICS, GREW FROM .3 SHARE IN JULY TO A .7 SHARE IN DECEMBER. DORAL HAS PROBABLY HURT THE GROWTH OF GENERIC SALES.

- CENTURY, ALSO INTRODUCED IN JULY, GREW TO .6 SHARE OF CIGARETTE SALES THROUGH HEAVY PACK/ CARTON TRIAL OFFERS.

- GENERIC SALES GREW +.6 SHARE (3.1 SHARE JULY TO 3.7 SHARE DECEMBER) BUT SUFFERED DURING SEPTEMBER AND OCTOBER FROM THE CONSUMER TRIAL OFFERS USED IN THE INTRODUCTION OF STRIDE, DORAL AND CENTURY.

- HALF OF ALL STRIDE SMOKERS CLAIM TO HAVE BEEN MARLBORO, WINSTON, SALEM OR KOOL CONSUMERS WHILE ONLY 5% SAID THEY WERE GENERIC SMOKERS.

WLM:BP

WHERE TASTE RUNS RICH

MEMORANDUM

February 26, 1985

TO: R. A. BLOTT

cc: L. W. Butler
H. C. Kerr
D. J. Dant

FROM: [Crossed Out]

SUBJECT: *GENERIC VERSUS FULL REVENUE PRICING COMPARISONS*

Since January, 1980, full revenue kings product has increased from a list price of $23.75 to $31.15 per M; that is an increase of 31.4%. During the same time-frame, generic prices increased from $14.95 per M to $18.75 per M, an increase of 25.4%

The attached analysis compares what has happened to retail carton and pack prices over that period of time. As you will note, this analysis uses average state taxes and standardized wholesaler and retailer markups.

Consequently, you should use the attached for directional advice only as the results will vary greatly depending on state taxes and customer markup policies. In general, however, the retail spread between generics and full revenue pricing has grown significantly over this period of time.

D. P. C.

/th
attachment

KING SIZE PRICING COMPARISON
Generics vs. Full Revenue

	JANUARY 1980		JANUARY 1981		JANUARY 1982		JANUARY 1983		JANUARY 1984		JANUARY 1985	
	GENERIC	FULL REVENUE	GENERIC	FULL REVENUE	GENERIC	FULL REVENUE	GENERIC	FULL REVENUE	GENERIC	FULL REVENUE	GENERIC	FULL REVENUE
List Price Per M	$14.95	$23.75	$16.40	$25.20	$16.40	$26.05	$17.25	$26.90	$17.25	$29.15	$18.75	$31.15
List Price Per Carton	$ 2.99	$ 4.75	$ 3.28	$ 5.04	$ 3.28	$ 5.21	$ 3.45	$ 5.38	$ 3.45	$ 5.83	$ 3.75	$ 6.23
Add Avg. State Tax	$ 1.10	$ 1.10	$ 1.12	$ 1.12	$ 1.14	$ 1.14	$ 1.16	$ 1.16	$ 1.18	$ 1.18	$ 1.20	$ 1.20
	$ 4.09	$ 5.85	$ 4.40	$ 6.16	$ 4.42	$ 6.35	$ 4.61	$ 6.54	$ 4.63	$ 7.01	$ 4.95	$ 7.43
Add 7% Wholesaler Markup	+ .29	+ .41	+ .31	+ .43	+ .31	+ .44	+ .32	+ .46	+ .32	+ .49	+ .35	+ .52
COST TO RETAILER	$ 4.38	$ 6.26	$ 4.71	$ 6.59	$ 4.73	$ 6.79	$ 4.93	$ 7.00	$ 4.95	$ 7.50	$ 5.30	$ 7.95
Add Retail Markup at 11%	+ .48	+ .69	+ .52	+ .72	+ .52	+ .75	+ .54	+ .77	+ .54	+ .83	+ .58	+ .87
CONSUMER COST PER CTN.	$ 4.86	$ 6.95	$ 5.23	$ 7.11	$ 5.25	$ 7.54	$ 5.47	$ 7.77	$ 5.49	$ 8.33	$ 5.88	$ 8.82
Difference Per Carton	$2.09		$1.88		$2.29		$2.30		$2.84		$2.94	
As A % of Full Revenue	(30.1%)		(26.4%)		(30.4%)		(29.6%)		(34.1%)		(33.3%)	
Estimated Cost Per Pack At 25%	$ .55	$ .78	$ .59	$ .82	$ .59	$ .85	$ .62	$ .88	$ .62	$ .94	$ .66	$ .99
Difference Per Pack	$ .23		$ .23		$ .26		$ .26		$ .32		$ .33	
As A % of Full Revenue	(29.5%)		(28.0%)		(30.6%)		(29.5%)		(34.0%)		(33.3%)	

BATUS[LOGO] A MEMBER OF THE BAT INDUSTRIES GROUP

BATUS INC.•2000 Citizens Plaza•
Louisville, Kentucky 40202 • (502)581-8000

HENRY F. FRIGON
President

March 5, 1985

Dr. I. W. Hughes
Brown & Williamson Tobacco
1500 B&W Tower
Louisville Galleria
Louisville, KY 40202

Dear Wally:

As you know, Charlie McCarty and I went to London the end of January to review the BATUS 5 Year Plan and Budget with the CPC. We have recently received BAT's comments on the discussions at that meeting, and I am enclosing the comments which are relevant to BATUS Corporate and to your operating group.

I do not think you will find anything particularly surprising but I did think you would be interested to see the type of discussions that take place.

Sincerely,

/s/ Hank

Henry F. Frigon

HFF:sr

cc: Mr. John Alar
Mr. T. E. Sandefur

Enclosure

* * *

Tobacco (Cont.)

8. It was agreed that the price of generics should be increased as soon as possible. B&W should be prepared to take the lead on this, while still retaining flexibility to discount the new prices if it became necessary to do so. A key condition for continuing to market generics was that B&W should be in a position to establish price leadership.

REDACTED

MEMORANDUM

To:	T. E. Sandefur, Jr.
CC:	J. Alar W. L. DeWitt I. W. Hughes C. J. Heger B. M. Lowdenback
FROM:	R. A. Blott
DATE:	March 6, 1985
SUBJECT:	Response to CPC Comments

REDACTED

REDACTED

* * *

8. It was agreed that the price of generics should be increased as soon as possible. B&W should be prepared to take the lead on this, while still retaining flexibility to discount the new prices if it became necessary to do so. A key condition for continuing to market generics was that B&W should be in a position to establish price leadership.

Response:

Brown & Williamson agrees with the C.P.C. viewpoint and would like to initiate a price increase as soon as we possibly can. The key element in leading the price increase, in B&W's judgment, is market strength. We believe that we will achieve that strength when we are confident that we are tracking toward the 8.6 billion target. Brown & Williamson should be in a leadership position from that point forward.

REDACTED

LIMITED

May be opened and seen
by addressee only

MEMORANDUM

To: ALL VICE PRESIDENTS

CC: J. Alar

FROM: T.E. Sandefur, Jr.

SUBJECT: *COMPETITIVE STRATEGY REVIEW*

DATE: March 21, 1985

Because of the increasingly competitive nature of the tobacco industry, each of you, working with your staff, is required to:

> Give consideration to the likely future moves by our competitors and the options open to B&W to either preempt or counteract them.

Direct your response to me in the following format by Friday, March 29.

- B&W's Options/Proposed Direction specify:
  - Strategies
  - General Tactics and Plans
  - Contingency Plans (i.e., including the circumstances under which these would be put into action)
- Comments on our Competitors include:
  - Specific tactics/plans you believe our competitors will follow over the next 12-18 months.
  - Alternative or additional strategic directions(s) [sic] for any of our competitors.

  - Any additions, changes and/or comments regarding the competitors; strengths and weaknesses listed.
- For your reference, the attached information summarizes our current assumptions regarding the competition, their likely strategies and some additional "thought starters."

/s/ T.E. Sandefur, Jr.
T.E. Sandefur, Jr.

/eah/0014/E

* * *

II. TOBACCO COMPETITORS: STRENGTHS, WEAKNESSES AND STRATEGIC DIRECTION

R.J. Reynolds

STRENGTHS

- Sheer size
- Strong sales force and merchandising program (e.g., fixtures, promotions activity)
- Balanced brand portfolio – best in the industry
- Strong position in production facilities. RJR will become a lower cost producer than B&W.
- A leader in commitments to R&D and Engineering
- Committed to continued investments to build the business through active new products and strong support of established products
- Greater manufacturing flexibility because of non-union shop
- Product quality – renewed emphasis
  - Physical – excellent
  - Smoking – parity
- A willingness to do the "uncoventional"

WEAKNESSES

- All brand families are declining.
- Emotional need to regain #1 position (i.e., at times reacts in a "knee-jerk" fashion)
- Quarterly loading practices for "public" reporting purposes generate significant cost inefficiencies.
- Geographical weakness in major metro areas
- Limited markets and brand portfolio in its International business
- Lack of depth of tobacco experience in senior management
- Biggest volume contributor to generics

STRATEGIC DIRECTION (RJR)

- RJR will aggressively pursue a leadership/grow [sic] position in all segments:
  - Price
  - Packaging
  - Female
  - Sizes
  - Styles
- In price segments, RJR is the most likely competitor to enter the black and white generic segment. They will also compete aggressively in mid-price point segments through either new products or conversion of existing brands.
- At the retail level RJR will fight and spend to maintain their existing dominant position in merchandising.
- RJR has geared up to develop a competitive edge on product development/R&D. They are the most likely competitor to develop a "health" product.

- RJR will be able to lead new product innovations and respond to new product opportunities more rapidly than other smaller competitors due to manufacturing capabilities and flexibilities. They will be the most active competitor in new brand activities.
- RJR has developed expertise and quality in packaging which they will use to gain competitive advantage (i.e., fresher products, potentially using some technology from its other food businesses).
- RJR will continue to maintain a leadership position in the area of special events, promotions, direct marketing, etc. This could be a great advantage if further restrictions are placed on traditional advertising methods.
- RJR will continue to assume a leadership role on public issues such as:
  - "Pride in Tobacco"
  - Tobacco support program
  - Smoking & health controversy
- RJR may well attempt to hold or limit their price increases in order to develop a competitive edge, as they are expected to be able to maintain their profitability through increased efficiencies and lower leaf costs. RJR might well attempt to use the fact that it did not increase prices on its product line when other companies did as a marketing tool. Or, RJR could selectively raise prices on only some of its established brands to provide increased profit generation and still "give the consumer a break."

- Internationally, RJR will:
  - Use pricing to penetrate and protect target markets.
  - Use competitive companies as vehicles to enter target markets (i.e., Argentina, South Africa).
  - Aggressively spend in high potential markets, such as Japan, with little regard for short-term profits.
  - Continue to aggressively push "transit" business
  - Continue centralization of decision making

Philip Morris

STRENGTHS

- Sheer size – both domestically and internationally
- Continued growth momentum in the Marlboro brand combined with its already powerful market leadership position
- PM has strong positions in segments which are growing:
  - Starters and younger adults
  - 100 mm
  - Full flavor (N/M)
  - Female
  - Box
- PM's product quality is:
  - Smoking – highest in industry and perceived by the consumer as excellent
  - Physical – parity

- PM is strong geographically in:
  - Metro areas
  - Northeast
  - West Coast
- PM has strong overall breadth and depth in its brand portfolio.
- PM has maintained consistency of marketing focus. Its Leo Burnett agency has excellent marketing/creative talents and strong tobacco experience. . . . "best in the industry".
- PM has concentrated on product technology (R&D, etc.) and production facilities. PM has made long-term financial investments/commitments to support these efforts.
- PM has the best efficiency in marketing spending.
- PM's large sales force represents a competitive advantage over those of smaller competitors.
- PM is on the leading edge of equipment acquisition and development.
- PM has aggressive, risk-oriented decision makers/takers.
- PM has the strongest and most profitable international business.

WEAKNESSES

- PM lacks menthol segment penetration and has no solo menthol brand.
- PM's field sales programs' execution and management skills are below average.
- PM has historically been slow to react to or engage in aggressive pricing.

STRATEGIC DIRECTION (PM)

- PM will aggressively attempt to penetrate the menthol segment. Its primary target appears to be KOOL.
- PM will not take a leadership position in low margin brand marketing.
- PM will make strong attempts to improve its position on shelving at the retail level.
- PM will further line extend existing products where possible (e.g., Marlboro Box 25's, B&H Box 25's, etc.).
- PM will maintain superiority on product smoking quality and improve the physical quality of its products. It is felt that PM will continue to generally follow product innovation rather than become the leader. However, PM will continue to maintain a leading position on smoking quality and work for technical breakthroughs to improve physical quality of products.
- PM will maintain a leading edge position on equipment through development/acquisition and will continue to spend to increase production efficiencies.
- PM will be the leader in image and pricing terms in the up market segments.
- Internationally, PM will intensify investments, especially in third world countries, with the objective of becoming the #1 cigarette company in the world. They are also expected to be actively pursuing new/growing opportunities in China and Eastern Europe. To expand its International business, PM is expected to continue to push its brands in even small markets without showing

profitable returns for a relatively long time in an effort to achieve its longer-term goals.

- PM will continue to maintain a leadership position in terms of its field sales force size and is expected to attempt to upgrade its field programs, execution and skill levels in the future.

Lorillard

STRENGTHS

- One growing trademark – Newport
- Product quality:
  - Physicial – above average
  - Smoking – parity
- Regional marketing strength and potentially some special "know-how"
- Willingness to make heavy investments/market spending in target markets
- Size of field force versus share
- Willingness to spend more for maintenance and quality within the manufacturing facilities at the "floor level".

WEAKNESSES

- Declining total market share and declining brand portfolio except Newport
- Lorillard's smoking quality of non-menthol brands is below average.
- Lorillard has had little recent product/new brand development success.
- Lorillard's primary stockholders are unwilling to allocate capital for new equipment or facilities.
- Inconsistency in brand communications

STRATEGIC DIRECTION

- Lorillard will drive Newport. They could become much more aggressive with this brand.
- Lorillard's new management could well be more aggressive and are expected to "try something" on the heels of the Newport's [sic] success. Other possibilities (excluding Newport) could be another female entry, a full flavor or a 100mm brand.
- Lorillard will continue to aggressively spend on media and field activities (i.e., above relative share).
- Lorillard is unlikely to enter the generic business.
- Lorillard will respond to the 25's full margin segment (i.e., possibly Newport 25's which would build starters).
- Lorillrd's staff is so lean that future tobacco experience and succession appear in jeopardy.

American

STRENGTHS

- Consistent strategy and maximization of cash flow
- Loyal franchise

WEAKNESSES

- A continued "milking" strategy produces a low level of spending in tobacco and insures continued market share and volume erosion of established brands.
- American's brand portfolio is weak and shows lack of growth potential.

- American shows a low level of new brand development and has had a lack of success with their recent attempts (i.e., Lucky).

STRATEGIC DIRECTION

- American is expected to follow basically the existing strategy for their current product line.
- American will selectively spend on brand-line extensions and new product opportunities that require small investments.
- American could provide contract manufacture for:
    - L&M
    - Coremark
    - Other private labels
- American will hold capital spending at a minimum level.
- American shows possible interest in selective international markets (Japan, etc.) for trademark development (i.e., Tareyton).
- American is felt unlikely to enter the black and white generic business.

L&M

STRENGTHS

- Leadership position in the economy segment (i.e., defended generic business to date and have the only mid-price product of the major competitors)
- Off-shore leaf facility

WEAKNESSES

- L&M's factory has older and slower speed equipment which is offset somewhat by slightly lower labor costs.

- L&M has poor quality of market share and a weak established brand portfolio.
- L&M's field sales force size is the smallest by a significant number.
- L&M has few R&D and product development facilities and human resources.
- L&M has limited cash/resource availability.

STRATEGIC DIRECTION

- L&M will try to survive by:
  - Raising prices on generics
  - "Sharing" the generic segment with B&W
  - Other niche marketing
    - Mid-price products
    - Ethnic products
- Grand Met will continue to try to sell L&M

LIGGETT & MYERS TOBACCO COMPANY, INC.
One North Park E., Suite 128, Dallas, TX 75231
(214) 369-7191

B. F. Ruggiero
Central Region Manager

DATE: April 2, 1985

TO: Leonard Browning
Bob Daugherty
Bob Dear

FROM: Bart Ruggiero

SUBJECT: Direct Account Business Presentations

I am forwarding a copy of an excellent presentation package put together by Jim Roe and his Managers comparing our Partnership in Profits Program with B&W's offers.

As you all know, B&W people have been hitting the trade quite heavy and distorting the truth with their presentations by indicating that they, the trade, will benefit greatly by changing from our generic product to theirs.

If the trade is not aware of our total program, including all incentives, rebates, promotions, etc., they can easily be mislead into believing that B&W has a solid program which is better than ours. Jim and his people have put together specific information for each of their accounts by using the attached guidelines. They have had success in reversing decisions made by the trade to go with B&W by using these business presentations.

Keep in mind that the attached is an example of how we can influence business decisions when we make the accounts knowledgeable and aware of our programs, which become more meaningful when can see documentation and comparisons.

We commend Jim and his people for developing an outstanding business presentation, which is the possible solution to combating B&W's thrust with direct accounts.

I would suggest you review the attached and develop a similar format for presentation where you feel it will be beneficial. If you have any questi [sic] please let me know.

BFR/mhw

cc: Dave Jackson
Mike Osborn
Jim Roe

MEMORANDUM

TO: J. ALAR
T. E. SANDEFUR
R. A. BLOTT
W. L. DeWITT
C. J. HEGER
B. M. LOWDENBACK

cc: B. E. Bacon
J. K. Wells

FROM: T. A. OLGES

SUBJECT: *CAC IX*

DATE: APRIL 9, 1985

For your reference, attached are the speech and support material compiled for Mr. McCarty's use at the CAC meeting.

/s/ Trina
T. A. Olges

/mjs/2791J

CAC IX

PHOENIX

BROWN & WILLIAMSON TOBACCO CORPORATION

APRIL 29 - MAY 2, 1985

*   *   *

TOBACCO BUSINESS: KEY ISSUES (SPEECH – H)

REDACTED

Because of the anticipation that the sunset provision will not operate and because tobacco will remain a target for revenue increases by all levels of government, B&W must further anticipate operating in price tiering is likely [sic].

In response to this issue, B&W established the following competitive pricing strategies to maintain and grow its volume without sacrificing profitability.

–

– B&W's entry and pricing policies within the generic and private label segment will attempt to maximize the profit opportunity available from this market segment. B&W's goal is to improve profits from this segment through a combination of significant production cost reductions and price increases. B&W would hope to reduce the spread between generics and full price productions if it could do so without reducing its share of this segment. B&W's presence within the segment appears to have resulted in reduced consumer advertising by L&M and a slowing in the segment's growth rate.

A major blend change on generics currently in progress will reduce costs by 95¢/1000 cigarettes. These measures will be coupled with Marketing's efforts to further develop more unique identity and equity characteristics in Brown & Williamson's black and white generic product line.

6: INTERMEDIATE PAGES REDACTED

CAC IX – PHOENIX
Brown & Williamson Tobacco Division

Table of Contents

15: INTERMEDIATE PAGES REDACTED

Competitive Pricing Strategy

B&W's competitive pricing strategies to maintain and grow its volume without sacrificing profitability are summarized by the following key directions:

REDACTED

-

- B&W's entry and pricing policies within the generic and private label segment will attempt to maximize the profit opportunity available from this market segment. B&W's goal is to improve profits from this segment through a combination of significant production cost reductions and price increases. B&W would hope to reduce the spread between generics and full price productions if it could do so without reducing its share of this segment. B&W's presence within the segment appears to have resulted in reduced consumer advertising by L&M and a slowing in the segment's growth rate.

-

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REDACTED

April 15, 1985

LIMITED

EXECUTIVE SUMMARY
LIGGETT ACQUISITION

A preliminary acquisition study of Liggett & Myers' cigarette business, including the Brazilian leaf processing business has been completed. The scope of the study included consideration of purchase price, earnings potential, asset valuation, working capital requirements, and synergistic savings. Ten scenarios were developed to recognize sensititivities [sic] relating to purchase price, generic volume, and branded volume. Considering the present condition of the business, the earnings potential, and the worth of the assets, it appears most likely that Liggett & Myers' business can be purchased for a price which will yield a high return.

Business Conditions

In early 1984, Grand Metropolitan announced negotiations were taking place for sale of the Liggett & Myers business to its management and some outsiders for $325 million, consisting of an undisclosed amount of cash and the assumption of certain debt. The sale was not carried out presumably from lack of available financing resulting from competition in the low cost cigarette segment. According to the 1984 Grand Metropolitan report, Liggett's operating income amounted to $77.9 million during the twelve months ended September 30, 1984. The report went on to state that profits have since been reduced to nominal amounts because of price incentives associated

with generic products which have been extended until June, 1985.

In 1984, Liggett sold 33.5 billion cigarettes or 5.7% of the total market. Their generic sales amounted to 23.9 billion units.

Recently, Grand Metropolitan announed [sic] its intention of selling its Pinkerton Tobacco business for an undisclosed sum.

Based upon the present business conditions, it appears that Grand Metropolitan would like to divest all its tobacco related operations. In fact, the purchase of Pinkerton (which was not studied) may be a condition for the purchase of Liggett.

Purchase Price

According to Grand Metropolitan's Form 10K for the twelve months ended September 30, 1983, Liggett's assets had a book value of $265 million. It is estimated this amount will increase $21 million to $286 million by January 1, 1986. Considering the asset values, the previous sale offering, and the condition of the business, time adjusted rate of return analyses were developed using purchase prices ranging from $225 million to $500 million.

LIMITED
May be opened and seen
by addressee only.

MEMORANDUM

[Handwritten]
file

TO: Mr. C. I. McCarty
Mr. H. F. Frigon

FROM: Mr. T. E. Sandefur, Jr.

DATE: April 19, 1985

RE: RICHLAND 250's National Launch and Proposed Generic Pricing Strategy

Per your request, attached is Brown & Williamson's rationale for the national launch of RICHLAND 250's and the Proposed Generic Pricing Strategy as discussed in New Orleans.

Should you need additional information, please let me know.

/s/ T. E. Sandefur, Jr.
T. E. Sandefur, Jr.

/eah

Att.

* * *

GENERICS

B&W's pricing strategy has been to take the leadership in announcing a price increase in 1985 provided we were tracking to the 8.6 billion unit volume objective for 1985.

As we are running behind our volume objectives, we are not in a position to lead a price increase and have, therefore, reassessed our pricing strategy.

It is our current belief that L&M, because of margin erosion will initiate a price increase on the order of $1.50 per M around mid-year, 1985. To generate volume and improve our market presence, our position is to hold off taking a price increase for three months from the time L&M announces. Having improved our market presence during these three months, we would initiate a price increase of $2.50 per M. We further anticipate that L&M, again because of margin erosion, would immediately increase their prices to parity with B&W. While such a strategy will negatively impact Trading Profit during the intervening three months, the additional volume generated and the higher level price increase will more than offset this negative impact in 1985.

The attached financial schedule indicates that successful implementation of this strategy, coupled with the benefits of the "low cost blend", will generate a positive 1985 Trading Profit of $9.6 million, $6.7 million more than budgeted. Preliminary calculations further indicate that 1986 Generic Trading Profit would increase significantly over the $14.0 million included in the Plan, on the order of a 100% improvement.

B&W's long-term strategies in Generics continue to be focused on margin improvement and to establish franchise equity through package design, etc.

4/19/85

[LOGO] Liggett & Myers Tobacco Company, Inc.

P.O. Box 60067, Sacramento, California 95860

June 21, 1985

Ted Winterhalder
Division Sales Manager

TO: All Sacramento S/Rs

FROM: T. Winterhalder

SUBJECT: *Price Increase*

As you know we raised our price on Branded & Generics/private label cigarettes. Branded by 20¢ per ctn. & Gneric [sic]/private label King 20¢ & 100's 25¢. This now makes the price uniform on the King & 100's by 20¢ & 25¢ respectively.

As of this date, Doral & B&W Generics have not indicated a price increase. We were forced to raise Generics simply because we are losing money which doesn't make good business sense. If our competitors want to lose money and/or lower the tobacco quality to gain SOM, that is fine but we do not have to. The 20¢ & 25¢ per ctn, is minor to the consumer but major to L&M. I have talked to three main jobbers in Reno, Nevada, & they think we are smart by raising the price on Generics. They all realize throught [sic] our debate programs we are making very little money if any. I also discussed in detail with each Direct Customer that it would make good sense not to have so many prices & recommended that they increase Doral & B&W if carried, with the same selling price as Gary Generics. As we discussed, if you do not take the price increase, the retailer will as they want to hold down the pricing categories due to clerk's & customer's confusion. My presentation made good business sense and all three

jobbers are now selling Doral & Generics for the same price. For your information, Glaser Bros. has a new private label brand called Major made by B&W. It is being sold to Glaser Bros. at the regular B&W Generic price, however, Glaser Bros. is selling Major for the same price as Best Buy, sold by Gary Tobacco.

You can see from the above we have taken a very positive position rather than a negative position. We are the inventors & leaders of Generic/private label cigarettes & have every intention of continued growth & SOM. Bottom line, B&W should not take away any Direct Customers from us as the jobbers are making the same profit whether it be Gary or B&W. Actually, the jobber would be losing money because he would be selling Doral & B&W Generic if carrying for the same price. By carrying Gary brand, he could then justify the Doral/B&W increase & make that extra profit rather than the retailer. As you can see, we have a good sould [sic] sales presentation & at the same time we can put Doral/B&W in a negative position.

B&W entered the Generic business because of our fast 6 to 9% SOM. They felt they had to cut prices in order to compete. All they did was make the low profit Generic segment non profitable. The Gary Generic concept is simple, quality tobacco, lower price & volume. But B&W wanted to give away all the profit to break open the market that we had 100% of. Their price cutting did not work as many warehouses in the United States still have B&W Generics that are 6 months & older. For your information, & all Direct Accounts, Gary Tobacco Co. is working on new merchandising programs to increase sales. We will advise you & our Direct Customers in 2 weeks.. So

advise all your Direct Accounts not to make any changes if they are contemplating one until they hear from you.

<u>Branded prices increase</u>

$1.00 per M = 20¢ per ctn. (King & 100's)

<u>Gary Tobacco price increase</u>

$1.00 per M = 20¢ per ctn. King Size

$1.25 per M = 25¢ per ctn. 100's

By Gary raising the 100's to $1.25 per M, there will be a uniform difference of 25¢ on all 100's.

cc: W.T. Lewis, File Copy

BATUS [LOGO] A MEMBER OF THE BAT INDUSTRIES GROUP

BATUS INC. • 2000 Citizens Plaza •
Louisville, Kentucky 40202 • (502) 581-8000

HENRY F. FRIGON
President
Chief Executive Officer

SECRET

July 18, 1985

Mr. G. L. Dennis
B.A.T. Industries, p.l.c.
P. O. Box 345 Windsor House
50 Victoria Street
London SW1H ONL
England

Dear Gerald:

In my absence earlier this week I understand you called and requested a note covering the details of the GPC contract (including the $20 million guarantee). I believe that all of the following information has been covered verbally with you and Eric Bruell in previous discussions, but we are happy to summarize this complex relationship and opportunity for you.

The trademark license with GPC offers a unique opportunity to deal with the two major concerns about B&W's generic business – the issue of equity in the product, and profitability. While there is very little equity in B&W's current black & white products, GPC accounts for almost one third of the generic market and represents significant equity. Sales of GPC cigarettes for the twelve months ended May 31, 1985, totalled 8.5 billion units, or 27% of that market. These GPC products are presently produced by Liggett and Myers.

Over the next 12 to 18 months B&W will gradually transfer a portion of its present black & white products to the GPC name, to bring about a dramatic reduction in the number of different labels which are produced – from about 40 in 1985 to only 8 by 1987. This will both build our equity in the GPC trademark and enhance manufacturing efficiencies.

With the addition of the 8.5 billion volume of GPC, B&W will be producing 2 share points or more under a single trademark. As the generic volume becomes this large it will be manufactured in long production runs at significant savings, achieving the same economic benefit as domestic manufacturing realizes versus export production.

The GPC volume will not require any incremental capital spending beyond that already projected in the 5 Year Plan, which is intended to support established brands but will also benefit generics. It will not be necessary to expand Macon capacity to accommodate the GPC volume.

The GPC organization will continue to be involved as a "broker" for GPC cigarettes and will help B&W sell and market GPC cigarettes to present and future GPC clients and customers. In addition, under the license arrangement GPC is excluded from doing work for any other tobacco company, which means they have to resign brokerage arrangements with Reemtsma for the "West" and "Astor" brands.

All cigarettes will be made to B&W's manufacturing specifications. B&W will have full control over specifications, marketing programs, prices, and terms and conditions of

sale for all GPC tobacco products. The license covers the entire tobacco products "category" and is worldwide. It will be a "category" exclusive to B&W, including any B&W affiliate(s) to whom B&W assigns rights. This flexibility may offer considerable advantages in the possible future use of the GPC trademark with Associate companies.

B&W will pay GPC a royalty of 15¢ per carton, 75¢ per thousand. We believe that this is a reasonable market rate within the Tobacco industry. On the basis of the current sales level of 8.5 billion, the first year payment would be $6.4 million. B&W has guaranteed a total minimum royalty of $20 million to be paid at a minimum rate of $4 million per year for each of the first five years of the contract. All royalties under the agreement are cumulative and once B&W has covered the total minimum guarantee of $20 million the minimum obligation terminates. Since B&W plans to convert existing generic volume to the GPC trademark, the annual royalty payments will probably exceed $8 million after the first year, and the minimum commitment will be met within three years.

You also raised the question of accounting treatment. There really is nothing unusual required by the contract unless, of course, for some unanticipated reason generic volumes fall more than 1/3 from present levels. The royalty will be charged against income as accrued on sales unless it becomes apparent that the minimum annual payment of $4 million will not be earned in the first five years. In that case, the annual charge to income would be $4 million.

Under the license agreement with GPC, which is for 35 years, B&W has the right to terminate the agreement at any time on 90 days' notice. However, the $20 million total minimum royalty must still be paid. This represents the one slight risk inherent in the contract.

If B&W is blocked from selling GPC cigarettes due to any actual or threatened legal or governmental action, the minimum royalty obligation shall be null and void from the outset until GPC resolves the pending matter.

GPC is obligated to prohibit *any* third party from causing a depreciation in value of the trademark until competitive GPC cigarettes disappear from the marketplace. B&W has rights of termination, rights to renegotiation and a right to void the minimum royalty obligation under this situation.

The GPC business provides B&W with considerably enhanced volume opportunities in generics. As we had anticipated, the rate of growth of this segment has slowed since B&W entered the market with generic products. With B&W's sales increased to one third of overall generic priced cigarettes, B&W will be in a much more competitive market position.

When all of these dimensions of the GPC contract are considered, I am sure you will understand our enthusiasm for the opportunity and our view that the risk is very low in comparison to the potential.

If you require further information, please let me know.

With kind regards,

Sincerely,

Henry F. Frigon

HFF:pjv

RICHLAND TRADE PRESS BRIEFING
Tuesday, July 23, 1985
North Casino Room
Marriott's Essex House
160 Central Park South
New York, NY

Order of Presentation

10:30 a.m.	All principals meet in the North Casino Room
11:00	Guests arrive to be greeted by J. S. Helewicz and representatives of Daniel Edelman, Inc. Brief introduction at that time to T. E. Sandefur and L. W. Butler. (Coffee and juice available)
11:15	JSH to open meeting, guests asked to be seated
11:20	Welcome B&W's purpose for hosting briefing a. Background on industry's rapidly changing environment and new trends b. Greater segmentation in the marketplace c. Richland's unique position against this background
11:25	JSH to introduce T. E. Sandefur
11:25	TES remarks (outlined in detail separately)
11:45	TES to close remarks JSH to acknowledge L. W. Butler JSH to open question and answer period
12:05 p.m.	Break Q&A period, guests asked to move to tables for luncheon

12:10	Bar opens
12:25	Lunch served
1:00	TES (option JSH) to wrap up by thanking guests for attending (suggest TES, LWB and JSH remain for any last minute questions)
1:30	Clear luncheon room

* * *

REGARDING PRICING, FIVE YEARS AGO A SMOKER PAID ROUGHLY THE SAME PRICE FOR CIGARETTES REGARDLESS OF BRAND. ONE KEY ON THE CASH REGISTER RANG UP ALL CIGARETTE SALES. WITH THE INTRODUCTION OF GENERIC CIGARETTES IN 1980 THIS CHANGED AS RETAILERS REQUIRED A SECOND TOBACCO PRICE TIER. SINCE THEN, ADDITIONAL PRICE TIERS HAVE EVOLVED AND THE BOOK ON CIGARETTE PRICING IS BY NO MEANS CLOSED. AS NEW PRODUCTS ARE OFFERED, THE RETAILER WILL FACE ADDITIONAL PRICING DECISIONS.